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Publications

GRAND TRUNK ARBITRATION

THE HONOURABLE SIR WALTER CASSELS, Chairman
RIGHT HONOURABLE SIR THOMAS WHITE, K.C.M.G.
THE HONOURABLE WILLIAM HOWARD TAFT

THE AWARD

AND

REASONS FOR AWARD

DELIVERED AT OTTAWA, THE SEVENTH DAY OF
SEPTEMBER, 1921



OTTAWA
F. A. ACLAND
PRINTER TO THE KING'S MOST EXCELLENT MAJESTY
1921

GRAND TRUNK ARBITRATION

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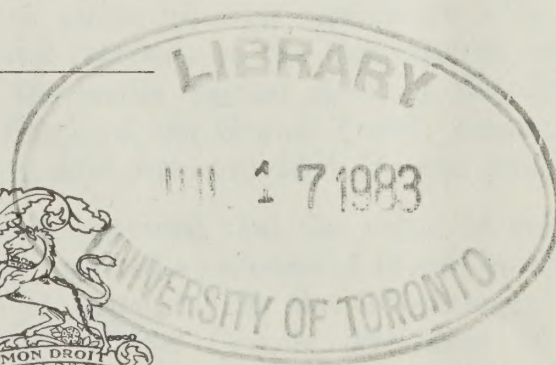
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GRAND TRUNK ARBITRATION

IN THE MATTER OF THE ARBITRATION

BETWEEN

HIS MAJESTY THE KING in right of the Dominion of Canada herein-
after called the "Government"

Of the First Part;

AND

IN THE MATTER of the GRAND TRUNK RAILWAY COMPANY OF
CANADA, hereinafter called the "Grand Trunk"

Of the Second Part.

BEFORE

The Honourable Sir WALTER CASSELS,
Chairman.

The Rt. Honourable Sir THOMAS WHITE, K.C.M.G., P.C.

The Honourable WILLIAM HOWARD TAFT.
Arbitrators.

OTTAWA, the seventh day of September, A.D. 1921.

AWARD

WHEREAS by 10 George V, Chapter 17, assented to on the 10th day of November, A.D. 1919, the Government was empowered to enter into an agreement with the Grand Trunk and with such other companies and interests as the Government might think necessary, for the acquisition by it of the entire capital stock of the Grand Trunk, except the four per cent Guaranteed Stock of the Grand Trunk, amounting to £12,500,000, upon the terms and conditions in said Act, provided for and enacted;

AND WHEREAS, by said Act it was, *inter alia*, provided that the value, if any, of the said stock of the said Grand Trunk so to be acquired as aforesaid should be determined by a Board of three arbitrators, one to be appointed by the Government, one by the Grand Trunk, and the third to be Sir Walter Cassels, President of the Exchequer Court of Canada;

AND WHEREAS, pursuant to the powers and authority given and conferred by the Act aforesaid, the Government entered into an agreement with the Grand Trunk bearing date the 8th day of March, A.D. 1920, whereby *inter alia* it was agreed by and between the parties hereto, that the Grand Trunk acting as aforesaid would use its

best endeavours to cause the sale and delivery to the Government, and the Government agreed to acquire the preference and common stock of the said Grand Trunk, the whole in the manner and on the terms and conditions set forth in said agreement;

AND WHEREAS it was further agreed in and by said agreement, that the value, if any, to the holders thereof, of the said stock, should be determined by a Board of Arbitrators as hereinabove stated, and that the said Sir Walter Cassels should be Chairman thereof;

AND WHEREAS the said agreement was duly ratified by the shareholders of the Grand Trunk, and was approved and confirmed, with some corrections as to the schedules, by 10-11 George V, Chapter 13;

AND WHEREAS, pursuant to the first mentioned Act and the said agreement, the Government then duly named and appointed the Rt. Honourable Sir Thomas White, K.C.M.G., K.C., as its Arbitrator on the Board of Arbitration aforesaid, and the Grand Trunk also named and appointed its Arbitrator on the said Board, namely, the Honourable William Howard Taft;

AND WHEREAS both the said Right Honourable Sir Thomas White and the Honourable William Howard Taft accepted the said office, and they together with the Chairman, Sir Walter Cassels, acted as such Arbitrators, forming the Board of Arbitration aforesaid;

AND WHEREAS, after due notice to the parties the said Board so constituted as aforesaid, met in Ottawa, and after hearing counsel, adjourned to hear evidence to the Board Room of the Grand Trunk in the City of Montreal, where on the first day of February, A.D. 1921, in presence of counsel for all parties, the hearing was resumed before the full Board;

AND WHEREAS by the agreement aforesaid, duly ratified in all respects, by said 10-11 George V, Chapter 13, it was further agreed and enacted that the award of the arbitrators, or a majority of them, should be made within nine months from the appointment of the arbitrators, or within such further time as the Governor in Council might approve;

AND WHEREAS WHEN said delay of nine months expired, the Grand Trunk had not concluded the presentation of its case, and in consequence no award had been made, the Board deciding they had no power to continue, adjourned *sine die*;

AND WHEREAS by 11-12 George V, Chapter 9, assented to on the 31st day of May, 1921, it was enacted that the Governor in Council, upon the Grand Trunk agreeing to further terms and conditions therein stated, might approve of a further time within which the arbitrators, or a majority of them might make their award, the Government and the Grand Trunk being respectively thereby authorized to agree for reviving and continuing the said arbitration, provided the agreement on the terms aforesaid were made on or before the 16th day of May, 1921, which said agreement was duly made and ratified, and an extension of the time duly approved;

AND WHEREAS by said Act it was further provided that in the event of the approval of a further time for making the award under the Act, or of any agreement concluded in pursuance of the powers thereby conferred:—"The powers and duties of the arbitrators shall remain and continue; and be deemed to have remained and continued, and the proceedings shall be resumed and concluded in all respects as if the time within which the Award is actually made had been the time limited therefor by the said agreement of the 8th March, 1920."

AND WHEREAS, in pursuance of said authority, the Board resumed its sittings at the City of Montreal aforesaid, after due notice, and in presence of counsel for both parties;

AND WHEREAS, both parties on Friday the 24th day of June, 1921, having declared their evidence closed, Thursday, the 30th day of June, 1921, was fixed for hearing argument;

AND the whole Board having on the said day and succeeding days heard the argument of counsel for all parties, and having also jointly heard all evidence adduced on the matters submitted for arbitration, the Board then reserved its decision;

Now we, the undersigned arbitrators, a majority of the Board, after mature deliberation and after careful consideration of the evidence adduced,

DO ORDER, AWARD, ADJUDGE AND DETERMINE that there is no value, to the holders thereof, in the "First," "Second" or "Third Preference Stock," or in the "Ordinary or Common Stock" of the Grand Trunk.

AS WITNESS our hands this seventh day of September, A.D. 1921.

(Signed) W. G. P. CASSELS,
Chairman.

(Signed) T. WHITE.

For reasons stated in a memorandum filed this day I dissent,

(Signed) WM. H. TAFT.

Witness to signatures of all three arbitrators,

(Signed) ARNOLD W. DUCLOS.

REASONS FOR AWARD

(By the Chairman, Sir Walter Cassels)

The importance of the questions raised in this Arbitration and the large sum of money involved render it proper to give my views on some of the questions raised.

The Board sat for 71 days continuously, except for the break between 8th April and 1st June, and ceased taking the evidence and hearing the argument on the 8th July.

I propose before discussing the construction of the agreement to deal with the surrounding circumstances leading up to its execution, in order to arrive at the true construction of the agreement.—*Burstall vs. Baptist 14 A.C., p. 13.*

Before doing so there are two questions raised by Counsel for the Crown, which I had hoped might not be necessary to be dealt with, but which I feel must be carefully considered.

The first point raised by Counsel is that the accounts of the Grand Trunk Railway System have been so manipulated—I use a milder term than that used by Mr. Tilley—as to render the accounts as presented by the books unreliable and unsatisfactory.

The second point is that for reasons of his own—I will quote later his own reasons as stated by himself—dividends were paid when, to the knowledge of the Chairman, there were no earnings applicable to the payment of such dividends; and those moneys so paid were diverted from paying claims due to the Government, which should have been paid, leaving the Government claim unpaid to the present time.

The Stock Exchange was notified. I have never thought the stock market quotations of any value in arriving at the question to be solved by the Arbitrators, but if the arguments put forward by Counsel for the Grand Trunk Railway have any weight, then the dealings referred to would effectually destroy any value to be derived from such quotations.

As far back as January 20, 1914, a cable is sent to London which reads as follows:—

“Preliminary figures for half year show \$566,000 or say one and a half per cent earned on third preference. To produce this result have increased item of General Interest wherever possible. That item now shows \$619,000 as compared with \$323,000 last year. If you approve will transfer to Operating Expenses \$290,000 same accounts as last year in order to improve comparison of general interest and operating expense account.”

This was done. The cable proceeds:—

“In case you wish to show two and a half per cent earned on third preference it will be necessary to reduce loss on Canada Atlantic by \$154,000 and carry in Canada Atlantic suspense, bringing total of that account to \$504,000.”

It is alleged by Counsel and not denied that this also was done.

McLaren is Chief Auditor to the Grand Trunk Railway. In 1919, according to his sworn statement there was a deficit of \$6,483,000. Instead of showing this deficit he shows a surplus of \$5,556.

I asked him this question:—

“Q. And that being a deficit, instead of showing a deficit of \$6,483,000, you show a surplus of \$5,556 and that is the same all the way through?”

His answer is:—

“A. Exactly.”

On December 10, 1915, Smithers wrote to Sir Robert Borden:—

“I told my colleagues that at the interview I had with you on March 26th, I had disclosed to you frankly the situation with which the Grand Trunk Railway and the Grand Trunk Pacific Companies would be confronted in the near future. I also told them that after full consideration and with the deepest regret I had proposed to you as the only safe solution of our difficulties, that the Government should take over the Grand Trunk Pacific Railway as from the 1st January next, with all its branch lines, together with its Development Company and other subsidiary companies with all the assets; the Grand Trunk Railway Company to surrender to the Government the whole of the common stock of the Grand Trunk Pacific Railway Company on condition of the Government relieving the Grand Trunk Railway of all liabilities in respect of the Grand Trunk Pacific Railway Company, its branch lines, its Development Company, and other subsidiary companies, and repaying to the Grand Trunk Railway Company any money advanced by the Grand Trunk Railway Company to the Grand Trunk Pacific Railway Company or its branch lines and Development Company and other subsidiary companies.

“In the course of conversation, as an alternative, you suggested that the Government might advance by way of loan sufficient money to supply any

deficiency in the amount required to meet the fixed charges of the G.T.P. Railway for the period of say five years anticipating that at the expiration of that period the net earnings would be sufficient for that purpose. I replied that under the present circumstances I did not think the Grand Trunk Railway Company would be justified in entering into any arrangement which would involve the accumulation of further liabilities against that company's revenues.

"I consider that any such arrangement involving such increased liabilities would so handicap the company's necessary powers of financing as to render it unable to fulfil the ever increasing demands of the public and public bodies; demands which could not possibly be met unless the credit of the Grand Trunk Railway was so maintained as to render possible the raising of fresh capital as required.

"My colleagues agree with the view I expressed to you and with the offer I made to you as expressed above, and which I now repeat with their concurrence. The liabilities of the Grand Trunk Pacific Railway Company will begin to accumulate as from the 1st January next as against net revenues, and any deficiency will have to be met by the Government and the Grand Trunk Railway Company. Under present circumstances, it is quite impossible for the Grand Trunk Railway Company to meet the extra liabilities arising from the Grand Trunk Pacific Railway Company.

"The amount of interest guaranteed by the Grand Trunk Railway Company is about \$2,750,000 annually to which must be added the interest on the amount spent on branch lines over and above the amount for which bonds have been or will be guaranteed by the Provincial Governments."

After referring to other matters he proceeds:—

"We have done our utmost to meet the heavy financing which has been necessary, and the difficulty of which has been immensely increased by the disastrous war conditions.

"We are now at the end of our tether with regard to Grand Trunk Pacific financing. The first Grand Trunk Pacific payments for interest after the 1st January next will become due on the 1st March, and amount to just under \$1,000,000 and there is no prospect of our being able to meet that payment."

The letter then concludes with regrets and so forth.

A series of cablegrams passing between Chamberlain and Smithers is produced. Chamberlain was then President of the Company.

January 28, 1917. Chamberlain to Smithers.

"Mr. Biggar thinks that unless Government waives its rights or gives consent, it would be improper if not illegal to pay dividends on the guaranteed stock or any preference stock without first making provision for payment of overdue interest on Government loans of 1909 and 1913 to the Grand Trunk Pacific, and also the guaranteed interest on Grand Trunk Pacific securities which rank ahead of the preferred stock. We were criticised by the Government for having paid last year on First Preference and if we were now to pay on First, Second and Third it would be impossible for us to get consent of Parliament for the increase we are asking."

Mr. Biggar, K.C., was at this time General Counsel for the Railway Company. On the 1st February, 1917, Chairman Smithers to Chamberlain:—

"Referring to your cable January 28, my view is Grand Trunk Pacific is being worked on construction account until by Order in Council it is declared open and operated on revenue account. That date has been postponed by agreement with Government from year to year and the Government

advance money from time to time. Our last expected time for opening would be January 1, 1916, but in anticipation of inability to meet liability we entered into negotiations with Government as summed up in my letter of December 10, 1915, to Prime Minister. The reply was Government would appoint Commission to advise on railway situation, and to carry Grand Trunk Pacific over interval. Government lent \$8,000,000 to provide 1916 interest in addition to other concessions mentioned in your letter May 3, especially Minister of Finance's statement he would forego interest on Government G.T.P. loans. Government thus waived its claim up to and including period covered by \$8,000,000. I would use every means to postpone any announcement which would embarrass your negotiations, but it appears to me legal position is net revenue results actually shown will have to be paid to preference shareholders in their order."

February 2, 1917, Chamberlain cables to Smithers:—

"Referring to your cable January 31, date of completion fixed by Parliament and not by Order in Council. Cap. 34 of Statute 1914 contains following:—

Notwithstanding anything contained in said Trust deed of 10th June, 1905, or any Act or Order in Council heretofore passed, the date for completion of Western Division shall be 31st day of December, 1915, and Government auditors insist upon accounts of company being kept on operating basis since that date.

"With regard to legal obligations to preferred stockholders, would call your attention to definition of net earnings set out in paragraph 18 of agreement of February 9, 1914, providing for amalgamation of Grand Trunk and Canada Atlantic, which amalgamation was confirmed by Act of Parliament, Chap. 89 of Statutes of Canada, 1914."

There could not be in the mind of any reasonable man a belief that net earnings mean anything but earnings after payment of interest on liabilities due.

9th of February, 1917, Smithers cabled Chamberlin:—

"Proposed to defer at all events publication of last year's revenue result until the Board meeting March 2nd. Please cable on receipt of my letter February 2nd preliminary figures before cabling statement to be submitted Board meeting. I am anxiously considering best course to pursue."

Cable is sent;—"Preliminary figures net amount available for dividends after charging up deficit on the D.G.H. and M. Railway and crediting surplus of G.T. Western Railway is £1,302,281.0s. 11d.

"Maintenance of Way expenses £909,214. 17s. 10d. against £1,002,729, 1s. 0d. in 1915.

"General Interest account credit of £234,615, 18s. 10d. against £95,870, 15s. 2d. in 1915.

"No charge made against Development Company for interest on advances in 1916 or against the Central Vermont Railway for advances for Southern New England road construction in same period."

McLaren's attention is called to the fact that his statement shows taken into Grand Trunk Railway of Canada £592,922, 17s. 0d. on account of interest on advance to the Development Company, and he explains;—

"It probably might have been placed in later." On February 20, 1917, Smithers cables Chamberlin:—

"Cable message received in regard to revenue results. Do you see any objection charging revenue with \$1,000,000 for maintenance of way showing the amount in the balance sheet as permanent way renewal funds. Have you any other suggestion to make?"

Chamberlin to Smithers, 21st February, 1917:—

"There would be no objection to charging to maintenance of way but we need rolling stock more than anything else. Our rolling stock stands on books \$55,000,000, and feel we should charge off two or three per cent annually for depreciation using same for renewals. Please cable which you will have it taken care of and amount."

February 22, 1917, Smithers cables Chamberlin:—

"Think Maintenance of way expenses should be increased \$500,000 to approximate 1915 figures showing amount in balance sheet as renewal fund and that a further \$600,000 be charged on account of rolling stock. Is there any objection to debiting general interest account with this \$600,000 to equalize them? Will not amount mentioned in your letter of August 21st be eventually used for rolling stock renewals?"

"Cable 23rd February, 1917, to London:—

"Have increased maintenance of way expenses \$500,000 and will reduce general interest by \$600,000. Amount mentioned in letter of August 21st can be used for rolling stock renewals. State what date you require usual cable." Then follows cable, Chamberlin to Smithers, February 26, 1917, informing Smithers; "Drayton-Acworth Commission with us and hope for favourable report" but proceeds as follows:—

"This expectation, however, will be entirely destroyed if you should pay dividends on anything more than First Preference. In my opinion, if anything more than that is done you must give up all idea of further relief in connection with G.T.P. at least for the present. Would also be advisable if possible to avoid publishing final figures net earnings at least until June."

On February 26, 1917, Smithers to Chamberlin:—

"Propose to pay full dividend of Grand Trunk Second Preference stock, which after charging amounts mentioned in your cable message of February will leave balance of \$280,000. The \$600,000 mentioned in that cable message should be included in accounts due by company and not included in any renewal funds."

"The balance of \$280,000 should be added to renewal funds and we must state in the dividend announcement that owing to the impossibility of obtaining necessary supplies and labour we have been unable to maintain as we should otherwise have done and the leeway will have to be made up at greatly increased prices and consequently we are carrying in the renewal funds about £400,000 which has been charged to working expenses. Please cable if you understand and your recommendations as to allocating the \$280,000, stating amount of each fund as it would appear on the balance sheet. If this is clear will cable further to-morrow and you can cable full statement Wednesday."

McLaren explains in reference to the item of \$600,000 that the accounts due by the company should be increased by \$600,000.

On February 27, 1917, Smithers cables Chamberlin:—

"Position is one of much difficulty. Will postpone announcement this week. Think it impossible to postpone publication of accounts as suggested. In view of net profits shown end of November shareholders expect dividends on Grand Trunk Second Preference Stock, Grand Trunk Third Preference Stock, so we must disclose we are holding balance. As mentioned in my cable message of yesterday, if we do not pay dividends on Grand Trunk Second Preference Stock, and so increase balance it will increase shareholders' dissatisfaction and render Board of Directors' position more difficult. If we do, however, and—dividend on Grand Trunk Second Preference Stock to balance on account of renewals will not Government say we must reserve amount for

1917 Grand Trunk Pacific Railway payments? Think I could carry proposal mentioned in my cable message yesterday with shareholders satisfied and if the Government objected we should show 1917 increased prices would absorb amount held over. Suppose we pay dividends on Grand Trunk Second Preference stock, and the Government then think we can take on liabilities of Grand Trunk Pacific Railway would not their view alter when they see how working expenses are increasing as will be shown in the monthly revenue statements? Dividend on Grand Trunk Second Preference Stock is only £125,000 and the answer to the Government would be we have no option according to Grand Trunk Acts and it is doubtful if we may not be compelled to pay Grand Trunk Third Preference Stock. Government must realize last year was quite exceptional. Will be pleased to consider further suggestion. Do not cable January working until results of last year published."

On February 27, 1917, cable from London:—

"In your last cable you set aside another \$500,000 which makes this account \$1,200,000 or £246,575 6s. 10d. This with the £280,000 now mentioned will give a total of £526,575 6s. 10d. instead of £400,000 as mentioned by you. Do you wish that only £400,000 should be shown as renewals, and the balance included in Preferred credit items, which is part of the accounts collectible?

"Would suggest that the renewal account covered by the £280,000 should be called "Engine and Car Renewal Account." So that it can be used for either engines or cars as necessary.

"Will include the \$600,000 in our Preferred Credit Items, so that it will not show in the Balance Sheet."

February 28, 1917, Chamberlin to Smithers:—

"Think we could probably get away with dividends on First Preference, but am very much afraid if you declare dividend on Second, Government will call on us to pay Grand Trunk Pacific interest. If any comment should be made relative to balance carried over, we could say that it was held to protect us for heavy expenses entailed this half year by severe winter, and abnormal increase in price of coal and other materials, while if paid out in dividends it would leave us without any excuse."

February 28, 1917, Smithers to Chamberlin:—

"Leave in the accounts collectible the amounts of \$500,000 and \$200,000 for maintenance of way renewals mentioned in your cable message of yesterday and charge the further \$500,000 for maintenance of way to working expenses, showing amount as special items in the balance sheet under head of maintenance of way renewal account. The £280,000 should be charged to working expenses and also shown in the balance sheet as special item under head of Engine and Car Renewal Accounts. Do not make these changes until we have agreed as to dividends on Grand Trunk Second Preference Stock in the light of my cable message of yesterday."

March 2, 1917, Smithers cables Chamberlin:—

"I have most anxiously thought of payment of dividends on Grand Trunk Second Preference Stock.

"I am certain non-payment after the showing to the end of November would create grave dissatisfaction among Grand Trunk shareholders and would doubtless result in agitation against Board of Directors and applications to the Courts. The relation of Board and shareholders here is quite different from what it is in America, *and one can suddenly drift into a very uncomfortable position.* If the Government complains we can urge the difficulty created by our special Acts of Parliament of Canada and that we did all possible by holding in suspense £400,000 when negotiations renewed. Our

monthly revenue statements will show this year, owing to heavy increase in working expenses, exceptional state of things last year. Hope you will be able to agree with me as to necessity of what I propose which Board approved after full consideration. Please cable."

9th March, 1917, Smithers to Chamberlin:—

"Referring to your cable of March 7th. Cannot understand Mr. Biggar's statement as to interest overdue to the Government on loans and guaranteed bonds. What amounts do you suggest are overdue and should be included in Grand Trunk accounts before the payment of dividends? How and when have they been formally demanded from the Grand Trunk Railway Company of Canada? In view of your letter of May 3rd cannot see how any amounts can be overdue. Cable particulars fully."

9th March, 1917, cable, Chamberlin to Smithers:—

"Your cable 9th. In July, 1915, the Government, by registered letter addressed to me as President of the Grand Trunk Pacific and as President of the Grand Trunk Railway Company of Canada, demanded payment of the sums of \$200,000 and \$300,000 respectively, being interest then due upon the \$10,000,000 advanced by the Government in 1909 on account of the Prairie Section and the \$15,000,000 advanced in 1913 on account of the Mountain Section. Payment of interest upon these advances was, as you know, guaranteed by Grand Trunk Railway Company of Canada. On 27th ultimo the Deputy Minister of Finance wrote Vice President and Treasurer Scott enclosing memorandum showing interest amounting to \$2,300,000 due by the Grand Trunk Pacific on these advances and asking to be advised as to the possibility of these amounts being paid in the near future. To this, reply was sent that there was no immediate prospect of interest being remitted. *All estimates sent you have shown as separate items interest due Government on these advances.*"

10th March, 1917, Smithers cables Chamberlin:—

"Confidential and unofficial. Sent yesterday cable message after long sitting with Committee of Board. We agree best course is to pay dividend on Grand Trunk Second Preference stock while holding in suspense £400,000 for renewal. I can get this through general meeting and *avoid serious agitation*. I feel sure, however, some of the Directors will not consent to this unless Mr. Biggar can modify his opinion. You see it even covers dividends on Grand Trunk First Preference Stock. If Mr. Biggar considers it absolutely illegal it appears to me only alternative will be to place much as possible to suspense for renewal and carry forward balance explaining that pending negotiations with Government we did not feel justified in dividing it. I fear Government would then claim amount but if it is not shown openly *shareholders would probably press for Committee of Investigation*. Reply to this and yesterday's cable message separately. Time short. We must make announcement March 16th."

March 12th, 1917, Chamberlin cables Smithers:—

"Mr. Biggar's view is that under the Act of 1862 dividends on the stocks in question are only payable in case sufficient 'net earnings' are available and that in arriving at 'net earnings' provision must first be made for payment of the amounts due the Government under the guarantees referred to. So long as you do not utilize in payment of those dividends moneys required to pay the Government should payment be insisted upon, the question of legality would not, in his opinion, arise."

March 12th, 1917, cable Smithers to Chamberlin, in which he refers to fact that dividends on guaranteed stock for 1915 paid without questions and so on, and suggests loan of \$8,000,000 cleared Grand Trunk Pacific until end of 1916, and shareholders so informed in notice to Stock Exchange.

Chamberlin replies by cable, March 13th, 1917, in which he points out that he never intended to convey the impression that interest was cancelled but only deferred for future consideration, etc. There are one or two further cables in the same line.

Finally on March 10th, 1917, Smithers cables Chamberlin:—

“Board have decided to pay Grand Trunk Second Preference stock dividend in full, reduce General interest by £100,000 and include amount in Preferred credit items as suggested in your cable message of February 27th, also debit net income account with £400,000 as a reserve towards meeting contingencies and possible liabilities showing amount specially in the general balances. Announcement published to-day.”

Dividends paid; unpleasantness to Directors avoided. Neither Sir Alfred Smithers nor Mr. Chamberlin were produced as witnesses on the part of the Grand Trunk Railway Company of Canada. Further comment is unnecessary.

The next question to be discussed is the effect of the evidence disclosed in the proceedings before what is commonly known as the “Drayton-Acworth Commission.” Considerable evidence was adduced before us and argument as to so-called “Deferred Maintenance Reserves.” I quoted on the argument two authorities, and repeat them.

“In the Supreme Court of the United States. *City of Knoxville vs. Knoxville Water Company*. 212 U.S. Rep. 2, at p. 13.

Mr. JUSTICE MOODY: The court refused to approve this method, and we think properly refused. A water plant, with all its additions, begins to depreciate in value from the moment of its use. Before coming to the question of profit at all the company is entitled to earn a sufficient sum annually to provide not only for current repairs, but for making good the depreciation and replacing the parts of the property when they come to the end of their life. The company is not bound to see its property gradually waste, without making provision out of earnings for its replacement. It is entitled to see that from earnings the value of the property invested is kept unimpaired, so that at the end of any given term of years the original investment remains as it was at the beginning.

It is not only the right of the company to make such a provision, but it is its duty to its bond and stockholders, and, in the case of a public service corporation, at least, its plain duty to the public. If a different course were pursued, the only method of providing for replacement of property which has ceased to be useful would be the investment of new capital and the issue of new bonds or stocks. This course would lead to a constantly increasing variance between present value and bond and stock capitalization—a tendency which would inevitably lead to disaster either to the stockholders or to the public, or both. If, however, a company fails to perform this plain duty, and to exact sufficient returns to keep the investment unimpaired, whether this is the result of unwarranted dividends upon over-issues of securities, or of omission to exact proper prices for the output, the fault is its own. When, therefore, a public regulation of its prices comes under question, the true value of the property then employed for the purpose of earning a return cannot be enhanced by a consideration of the errors in management which have been committed in the past.”

And in a case decided by Jessel J., then Master of the Rolls, pertinent language on the same point is used. This was a case in which an application was made to

restrain payment of dividends, the contention being that profits had not been made entitling the company to the payment of dividends.

In delivering judgment, Jessel, J., Master of the Rolls, used the following language:—

“Then I have to consider the question, What are net profits? A tramway company lays down a new tramway. Of course the ordinary wear and tear of the rails and sleepers, and so on, causes a sum of money to be required from year to year, in repairs. It may or may not be desirable to do the repairs all at once; but if at the end of the first year the line of tramway is still in so good a state of repair that it requires nothing to be laid out on it for repairs in that year, still, before you can ascertain the net profits, a sum of money ought to be set aside as representing the amount in which the wear and tear of the line has, I may say, so far depreciated in value as that that sum will be required for the next year or next two years. Take the case of a warehouse. Supposing a warehouse-keeper, having a new warehouse, should find at the end of the year that he had no occasion to expend money in repairs, but thought that by reason of the usual wear and tear of the warehouse, it was £1,000 worse than it was at the beginning of the year, he would set aside £1,000 for a repair or renewal or depreciation fund before he estimated any profits; because, although that sum is not required to be paid in that year, still it is the sum of money which is lost, so to say, out of capital, and which must be replaced. I should think no commercial man would doubt that this is the right course—that he must not calculate net profits until he has provided for all the ordinary repairs and wear and tear occasioned by his business. In many businesses there is a regular sum or proportion of some kind set aside for this purpose. Ship-owners, I believe, generally reckon so much a year for depreciation of a ship as it gets older. Experience tells them how much they ought to set aside; and whether the ship is repaired in one year or another makes no difference in estimating the profits, because they know a certain sum must be set aside each year to meet the extra repairs of the ship as it becomes older. There are very many other businesses in which the same thing is done. That being so, it appears to me that you can have no net profits unless this sum has been set aside.”

Other authorities to the same effect were cited by Mr. Butler in his argument to the Board.

Following the letter of the 10th December, 1915, the Commission was appointed to enquire into the whole railway situation, and material evidence under oath was given by Mr. Chamberlin, President of the Grand Trunk Railway Company of Canada, and of the Grand Trunk Pacific, and corroborated by Mr. Kelley, then Vice President and Chief Engineer.

There has been no attempt to vary this evidence. Mr. Chamberlin was not produced as a witness in the Arbitration proceedings; and Mr. Kelley, although on the stand for several days, was not questioned in regard to these statements. I quote some parts of this evidence. Sir Henry Drayton asked Mr. Chamberlin the following questions:—

“There is one other matter; you think that the Government as a matter of fairness to the Grand Trunk, ought to relieve the Grand Trunk Railway Company of its total Grand Trunk Pacific investment?”

“Mr. CHAMBERLIN: I do.

“Sir HENRY DRAYTON: And repay to the Grand Trunk the money it has in the Grand Trunk Pacific, and relieve the company of all its responsibilities. That is a large order. We want to give you every opportunity to state every ground on which you think that should be done.

"Mr. CHAMBERLIN: Well, Sir Henry, if you will look at this map, you will see where the Grand Trunk Pacific stretches away off up through the north country, while the Grand Trunk is away down in this part of the country. It is not a natural connection of the Grand Trunk is it? It is not only not a connection with the Grand Trunk but it is not of any benefit to the Grand Trunk.

"In the first place, we are under contract to send all business over this north line, away from the Grand Trunk. The Grand Trunk cannot derive any benefit from it, under the contract with the Government.

"Commissioner ACWORTH: That is a new point, to me.

"Mr. CHAMBERLIN: In addition to that, the company is bound to put steamers on the Atlantic and steamers on the Pacific, to accommodate all that business, and yet it does not bring one dollar of business to the Grand Trunk.

"Commissioner ACWORTH: How does that obligation arise?

"Mr. CHAMBERLIN: It arises out of the contract with the Government.

"Commissioner ACWORTH: The original contract with the Government?

"Mr. CHAMBERLIN: The original contract.

"Mr. BIGGAR: Of July 29, 1903.

"Commissioner ACWORTH: Is the agreement a schedule to the Act?

"Mr. BIGGAR: Yes, sir, a schedule to the Act of 1903. Chapter 80, I think it is.

"Commissioner ACWORTH: Therefore, if the Grand Trunk, as it does at present, operate or control the operation of the Grand Trunk Pacific, were to send traffic through Portland instead of through Halifax, it would be a fraud on the agreement?

"Mr. CHAMBERLIN: Yes. We are bound to go on with all that tremendous outlay and to carry that load, and yet not get one dollar of benefit from it. The Grand Trunk simply cannot carry it.

"Commissioner ACWORTH: Let me ask this question; when you went away from the agreement to work the Transcontinental, was that question of the obligation of the Grand Trunk Pacific to carry over the Transcontinental ever raised?

"Mr. CHAMBERLIN: No. The agreement is with the Grand Trunk Pacific, not with the Transcontinental.

"Commissioner ACWORTH: But it was practically Grand Trunk, rather than Grand Trunk Pacific.

"Mr. CHAMBERLIN: It is in the name of the Grand Trunk Pacific, not of the Grand Trunk.

"Commissioner ACWORTH: The Grand Trunk Pacific said they could not work the Transcontinental with its present cost?

"Mr. CHAMBERLIN: Yes.

"Commissioner ACWORTH: And the Grand Trunk Pacific did not raise, and the Grand Trunk was not in a position to raise—that is what it comes to—the question of whether the obligation remaining on the Grand Trunk Pacific to run over the Transcontinental was a reasonable one?

Mr. CHAMBERLIN: Well, it was not raised, anyway.

"Commissioner ACWORTH: I am an outsider in regard to these matters and have to pick them up as we go along.

"Mr. CHAMBERLIN: The only body that could raise that question would be the Government, I should say.

"Mr. BIGGAR: The only company which could raise any objection would be the Grand Trunk Pacific.

"Commissioner ACWORTH: An obligation to operate *via* Halifax rather than *via* Portland is an obligation of the Grand Trunk, not of the Grand Trunk Pacific?

Mr. BIGGAR: Yes. It is provided for in the agreement dated the 29th of July, 1903, which is a schedule to chapter 71 of the Statutes of Canada, 1903.

“Commissioner ACWORTH: The Act constituting the system?

“Mr. BIGGAR: An Act confirming an agreement entered into between His Majesty the King and Sir Charles Rivers Wilson and others acting on behalf of the Grand Trunk Pacific Railway Company.

“Clauses Nos. 41 to 45, inclusive, provide:—

“41. At all times during the terms of the said lease the company shall continuously and efficiently operate both divisions of the said railway, giving due and sufficient service for the accommodation of all traffic to the satisfaction of the Government.

“42. It is hereby declared and agreed between the parties in this agreement that the aid herein provided for is granted by the Government of Canada for the express purpose of encouraging the development of Canadian trade and the transportation of goods through Canadian channels. The company accepts the aid on these conditions, and agrees that all freight originating on the line of the railway, or its branches, not specifically routed otherwise by the shipper, shall, when destined for points in Canada, be carried entirely on Canadian territory, or between Canadian inland ports, and that the through rate on export traffic from the point of origin to the point of destination shall at no time be greater *via* Canadian ports than *via* United States ports, and that all such traffic, not specifically routed otherwise by the shipper, shall be carried to Canadian ocean ports.

“43. The company further agrees that it shall not, in any matter within its power, directly or indirectly, advise or encourage the transportation of such freight by routes other than those above provided, but shall, in all respects, in good faith, use its utmost endeavours to fulfil the conditions upon which public aid is granted, namely, the development of trade through Canadian channels and Canadian ocean ports.

“44. In respect of the tolls for any traffic carried partly over any line of railway operated by the company and partly over any of the lines of the Intercolonial railway, a fair and equitable rateable division of all such tolls shall be made by mutual agreement, or, in case of dispute, such division shall be fixed by arbitrators appointed in the manner provided by paragraph forty-seven of this agreement, or by a Board of Commissioners which may hereafter be duly appointed as mentioned in paragraph nineteen of this agreement, and with the right of appeal as therein mentioned.

“45. The company shall arrange for and provide, either by purchase, charter or otherwise, shipping connections upon both the Atlantic and Pacific oceans sufficient in tonnage and in number of sailings to take care of and transport all its traffic, both inward and outward, at such ocean ports within Canada, upon the said line of railway, or upon the line of the Intercolonial railway, as may be agreed upon from time to time, and the company shall not divert or, so far as it can lawfully prevent, permit to be diverted, to ports outside of Canada any traffic which it can lawfully influence or control, upon the ground that there is not a sufficient amount of shipping to transport such traffic from or to such Canadian ocean ports.

“Mr. CHAMBERLIN: We are bound to make the same rates from Halifax and St. John as are made to Boston and Portland, and we are bound to provide steamships on the Atlantic and on the Pacific to take care of any business offering.

“Commissioner ACWORTH: You never have provided ships on the Atlantic, in fact?

“Mr. BIGGAR: No.

"Commissioner ACWORTH: And the Government has never called on you to carry out your contract?"

"Mr. CHAMBERLIN: You talk about the money the Government would have to raise to pay off the Grand Trunk. They would not have to raise \$250,000. This has been financed on a three and four per cent basis except on loans from the Government, and I have offered to take the advances in Government bonds of ten or fifteen years.

"Sir HENRY DRAYTON: But the obligation is there the burden is there, and the carrying costs are there.

"Mr. CHAMBERLIN: Yes, but it is really a matter of financing, to-day.

"Sir HENRY DRAYTON: Your first point, Mr. Chamberlin, is that the Grand Trunk is not interested in all this development at all, and that the railway as contracted for and laid out is something which takes traffic away from the parent Grand Trunk System instead of giving traffic to it.

"One answer that might be quite easily made to that is that the representatives of the Grand Trunk must have known all that when this contract was entered into?"

"Mr. CHAMBERLIN: I don't know. They must have. Of course, I do not want to criticize my predecessors."

(p. 81).

"Sir HENRY DRAYTON: You speak of confiscation, in your letter, Mr. Chamberlin. No person is thinking of confiscating the investment that I know of. If you can afford to carry it, you will be allowed to carry it. That was not really meant, was it? Suppose you are left to yourselves, *the thing crashes*, no one confiscates it. Isn't that right?"

"Mr. CHAMBERLIN: To a certain extent, yes.

"Sir HENRY DRAYTON: To every extent, isn't it?"

"Mr. CHAMBERLIN: To every extent.

(p. 82).

"Sir HENRY DRAYTON: You also mention in your letter that the money was put into the undertaking in good faith, and that it was a national undertaking. We have to look upon that more or less in the way these large terms are usually taken. It is only national to the extent that the agreement makes it.

"Mr. CHAMBERLIN: Of course we are very anxious to avoid a break or a *crash*. The Grand Trunk has to raise a great deal of money, as you know in your Department, for grade separations, improvements to hotels, etc.

"Sir HENRY DRAYTON: I quite agree with that. You should be able to raise a great deal of money for the purchase of rolling stock and so on.

"Mr. CHAMBERLIN: We have to. Of course the debenture stock is a first Lien, and these guarantees are right behind the debenture stock.

"Sir HENRY DRAYTON: Your point, I take it, is that it is impossible for the Grand Trunk to continue its service and raise money, under these circumstances.

"Mr. CHAMBERLIN: Absolutely.

"Mr. CHAMBERLIN: The idea is that if the Grand Trunk and the Grand Trunk Pacific *go into insolvency—which they will have to do* if the Grand Trunk attempts to carry out that arrangement—the Grand Trunk Pacific having been heralded and looked upon as a Government backed road, it would naturally have an effect upon the other securities as well."

(p. 83).

"Sir HENRY DRAYTON: Doesn't it really come down to this, that the statements in your letter mean that in your view, in order to protect the finances

of the Grand Trunk, and as a corollary to protect the finances of the country, the Government ought to relieve the Grand Trunk in regard to its investment; isn't that the whole thing?

"Mr. CHAMBERLIN: That is the whole thing.

"Sir HENRY DRAYTON: There is nothing else to it?

"Mr. CHAMBERLIN: Nothing else.

"Mr. CHAMBERLIN: The fact is that the Grand Trunk is not able to contribute anything towards paying its own security holders and making the improvements the people of Canada demand and the business of Canada requires.

"Sir HENRY DRAYTON: But last year the Grand Trunk gave its shareholders half a million sterling?

"Mr. CHAMBERLIN: Yes."

(p. 84, line 1).

"COMMISSIONER ACWORTH: To say to the Grand Trunk that they must pay these liabilities to whatever extent they can, because as far as the public was concerned the Government would have to face the rest, but that the Grand Trunk must do all it can.

"Mr. CHAMBERLIN: The Grand Trunk can just about meet it, but cannot pay the shareholders anything.

"COMMISSIONER ACWORTH: It divided a profit last year of \$2,500,000?

"Mr. CHAMBERLIN: You do not call it munificent, to pay interest on your guaranteed securities, do you?

Commissioner ACWORTH: But guaranteed stock is a share, not a bond. Are we agreed upon it, that the company divided a certain amount last year as a profit, a profit dividable as a dividend?

"Mr. CHAMBERLIN: How about the first, second, and third Preference stocks?

"COMMISSIONER ACWORTH: Those holders would not get anything. For a series of years there has always been some amount paid as dividend?

"Mr. CHAMBERLIN: We would not have paid so much last year, if we had paid out on the Grand Trunk as much as we ought to have paid for betterments.

"Sir HENRY DRAYTON: If you had paid all you should have paid out for betterments, you would not have been likely to have paid anything?

"Mr. CHAMBERLIN: No. We have not put in any rails for two years past, of any account.

"Sir HENRY DRAYTON: How much do you think you should put in, to keep things right, in order to look after proper operation?

"Mr. CHAMBERLIN: We should have at least three and perhaps four per cent put aside every year on rolling stock. That would amount to from \$2,000,000 to \$2,500,000.

"Sir HENRY DRAYTON: You have never done that?

"Mr. CHAMBERLIN: We have never done that. I have had it before the Board, and have practically insisted upon it being done whenever we get any new rolling stock. I bought about 10,000 cars the first year I was here. They were all charged to capital account. We should have had a reserve fund for taking care of them. We now have to go and do the same thing over again.

"Sir HENRY DRAYTON: Supposing you were to reconstruct your accounts now; I want to see what effect these items would have on the Grand Trunk. What would the providing of three or four per cent annually amount to?

"Mr. CHAMBERLIN: My idea is that it would take five per cent. Take engines and cars, they are either worn out or out of date in twenty years.

"Sir HENRY DRAYTON: I agree with you absolutely. If you were to tell your accountants to go and make provision of that kind in respect of your equipment, on that basis, it would preclude the shareholders from receiving anything for years and years?

"Mr. CHAMBERLIN: You mean, if we made it up for back years?

"Sir HENRY DRAYTON: Yes.

"Mr. CHAMBERLIN: Yes, it would. It would mean \$2,750,000 a year.

"Sir HENRY DRAYTON: You would have to go back probably twenty years to make it right.

"Mr. CHAMBERLIN: Yes.

"Sir HENRY DRAYTON: To put your accounts in proper shape, in regard to a proper equipment, would require a reserve of \$25,000,000.

"Mr. CHAMBERLIN: Take the matter of grade separation at Toronto, for instance.

"Sir HENRY DRAYTON: Suppose you suggest \$27,000,000—wouldn't \$25,000,000 be enough to properly provide for reserves for equipment?

"Mr. CHAMBERLIN: Yes, I think it would. We have now a lot of new equipment charged to capital; if we had \$25,000,000 now, it would put us in fine shape."

(P. 85)

"COMMISSIONER ACWORTH: I don't know about 1916, but even in 1915 you did not put in very many new rails?

"Mr. CHAMBERLIN: No, we did not.

"COMMISSIONER ACWORTH: And did not make a reserve for the money you would have spent if you had got the rails?

"Mr. CHAMBERLIN: I do not mean to say that the rails are dangerous. But we must put in a certain percentage every year. If we go over a couple of years, the first thing we know we will have a lot of rotten rails."

Next in order is Mr. Kelley's statement in answer to Sir Henry Drayton. See Exhibit No. 444. I quote from the Drayton-Acworth Report at page xxxiii. The details are fully set out in the Exhibit referred to.

"The Vice-President in charge of operations, Mr. Kelley, has direct responsibility for the plant. On Mr. Chamberlin's evidence being put to him, he agreed with it. He has since submitted to us a full report on the question of Deferred Expenditure. 'Deferred Expenditure' means, in plain English, expenditure which has not been made, but which, in view of those charged with the duty of maintaining the plant, ought to have been made.

"We give below Mr. Kelley's summary in tabular form, but we do not think it necessary to reproduce all the supporting tables.

"GRAND TRUNK RAILWAY SYSTEM"

SUMMARY OF DEFERRED EXPENDITURES

Rebuilding and reinforcing freight car equipment.. . . .	\$ 8,943,971.14
Rebuilding freight and passenger cars with safety appliances—	
Original estimate.. . . .	\$850,722.50
Already expended.. . . .	392,220.89
Balance to be expended.. . . .	458,501.61
Equipping engines with safety appliances—	
Original estimate.. . . .	\$ 17,828.00
Already expended.. . . .	553.68
Balance to be expended.. . . .	17,274.32
Deferred renewals in Maintenance of Way Department—	
In Canada.. . . .	\$6,182,672.00
In United States.. . . .	5,578,926.00
	11,761,598.00
Total.. . . .	\$21,181,345.07

MONTREAL, March 5, 1917."

"On the single item of 'rails' the 'cash expenditure required to restore to normal conditions' is reported as \$5,312,142. The cost of restoring ballast to normal conditions is reported as \$2,434,000.

"With reference to the Deferred renewals in Canada amounting to over \$6,000,000, it appears that they have accumulated during 11 years, 1906-16. During this period, in spite of the requirements of the property, and the claims of public safety, \$36,000,000 were paid out in dividends.

"The \$21,000,000 dealt with above represent the money which the responsible officers of the company estimate to be required to put the existing plant into good normal condition. This is a revenue liability. But the existing plant is quite inadequate for existing traffic and requires large additions, for which new capital must be raised. The estimates of necessary capital expenditure submitted to us are as follows:—

Requirements for rolling stock, shops and machinery....	\$26,150,000
Requirements for automatic block signals (main line in Canada only).....	3,533,000
Requirements for installing rock ballast crushing plant..	467,500
Total.....	<u>\$30,150,500</u>

Putting together revenue and capital expenditure, we find that the Grand Trunk Railway, in the opinion of its own officer, requires over \$51,000,000 spent upon it to put it in a position to meet the requirements of its to-day's business. We see no reason to expect that under existing conditions this necessary money will be provided.

Before dealing with the correspondence leading up to the agreement and the meaning of the agreement, it may be well to refer to what is called "The Budget." It throws light on the financial position of the Grand Trunk Railway System. The Budget is contained in exhibit 475. It is headed:—

- "The Grand Trunk Railway System.
- "Estimated Cash Requirements including Capital.
- "Expenditure, meeting obligations, etc.
- "January 1, 1921, to March 31, 1922."

The grand total is \$89,687,633.39.

It is only necessary to consider the enormous outlays necessary, to understand how futile it is to expect a railway to pay dividends unless material outside assistance is furnished.

It is unnecessary to set out in detail the items of requirements for the fifteen months from January 1, 1921, to March 31, 1922. Exhibit 475 contains the information in full.

I proceed now to give my views as to the construction to be given to the agreement. In the opinion pronounced on February 7, 1921, I declined to acquiesce in the argument of Mr. Lafleur that the Statute in question was a forcible expropriation of the three Preference Stocks and the Common Stock.

After hearing further argument by Counsel for the Grand Trunk Railway and the Crown, I am convinced that the view I formed is correct. The correspondence printed regarding the Grand Trunk Railway acquisition, and the facts leading up to the agreement, demonstrate that the shareholders were quite free to enter into an agreement or not as they thought best in their own interests. It is apparent that the Grand Trunk Railway were at the end of their tether and without assistance could not carry on; and, aware of this fact, the Company endeavoured to obtain the best price possible for the sale of their undertaking.

In 1919, Chapter 17, George V, was enacted, which authorized the Government and the Grand Trunk Railway to enter into an agreement by which the Crown would

acquire and the Grand Trunk Railway of Canada would sell the whole Grand Trunk Railway System to the Crown on the terms set out in the Statute.

There was no compulsion or forcing of the Grand Trunk Railway shareholders to enter into the agreement; they were free agents and as such voted in favour of the agreement, and thereupon the agreement of March 8, 1920, was entered into by the Crown and the Company.

Under the terms of this agreement the Crown assumed large liabilities of the Grand Trunk Railway System from the date of the appointment of the Committee of Management, May, 1920.

The contention on the part of the Crown was that they had agreed to pay full and adequate compensation, and that there was no value in the first, second and third Preference stocks or in the common stock of the Grand Trunk Railway Company of Canada.

The Grand Trunk Railway Company of Canada, on the other hand, contended that there was value to the holders of the first, second and third preference and common stocks, and the agreement provided for this Arbitration to determine what, if any, sum should be paid to the stockholders.

If the Board of Arbitrators find any sum due this amount is to be satisfied by guaranteed stock bearing interest at four per cent, such interest dating back to the date of the appointment of the Committee of Management, namely, May, 1920, the date when practically the sale and purchase was completed.

It is a common form of agreement for a vendor to agree to sell and a vendee agree to buy for a price to be settled by arbitration. In the Court of Chancery in Ontario and I think in England it is common practice to obtain a vesting order where a vendor refuses to carry out the terms of a judgment ordering him to convey the property.

In this case, whether any amount is awarded or not, the four classes of stockholders have agreed to assign their stock.

Coming now to the construction of Clause 6 of the agreement of the 8th March, 1920:—

“The value, if any, to the holders thereof”; I am of the opinion that “value” means the “intrinsic value.”

The cases cited by Mr. Tilley, *Peake vs. Derry*, etc., are very much in point. All the negotiations are based on earning power, and it was the intrinsic value the parties evidently had in view.

Watcham vs. Attorney General E.A. Appeal Cases 1919, p. 538. And for the reasons given the quotations of the Stock Market would form no criterion.

I now proceed to deal with the important question, the subject matter of the decision of the 7th February, which decision *seemed* to afford considerable dissatisfaction to the counsel for the Grand Trunk Railway Company. I see no reason whatever to doubt the correctness of the view I then formed, and I do not wish to repeat the reasons I then gave.

Throughout the proceedings Counsel constantly referred to this decision as “the majority decision.” This is incorrect. So far as the principle or basis of compensation is concerned, the Board are unanimous. My friend Mr. Taft, who is quoted as “the dissenting Arbitrator,” is, if the record is correct, fully in accord with the views expressed by Sir Thomas White and myself. I quote his language:—

“Without saying that market quotations may not be submissible, it is clear that we must look for other means of determining the issue here. The whole stock of the railway is valuable or otherwise as the ownership and control of the physical property of the railway as a going concern in the discharge of its public duties will enable it to earn a sufficient amount to pay dividends on the stock. We are, therefore, to capitalize its net earning capacity, present and potential, and fix the value of the stock on that basis. Its earning capacity, present and potential, is what is now earned and what it

may be expected to earn under reasonable probable conditions. Net earnings are the revenue received less the operating expenses. What determines the revenue of a going railway are the amount of its business and the rates it can charge."

During Mr. Tilley's argument for the Crown, the following remarks of Mr. Taft indicate a complete accord with the views of the majority (p. 7676):—

"Hon. Mr. TAFT: Mr. Tilley, we are here to determine the value of this road, this Company's property, and we are using these accounts to find out what its earning capacity was during these various years. We also have to take into consideration what its liabilities are; what its permanent liabilities are. These seem to be, so far as the Grand Trunk Pacific is concerned, something like \$3,700,000."

Again at page 7678:—

"Hon. Mr. TAFT: The question of the operating income; the net operating income is the basis on which we must calculate the value of this road, reduced by what its liabilities may be in the future."

The point of difference was to the reception of certain evidence. This evidence, according to the view of Mr. Taft, might be of value as indicating a probable increase of rates by the Interstate Commerce Commission.

Under Clause 7 of the agreement, the Arbitrators, or a majority, have sole discretion as to the admission of evidence, and if the majority are of opinion that no amount of evidence of the character offered would effect their opinion, surely it was their duty to rule it out and save an enormous amount of expense and delay. Besides, if what the Board consider is the correct principle upon which the valuation has to be made, namely, earnings, how can it possibly affect the case what the reproduction cost might be? The question that might come up before the Interstate Commerce Commission is not merely the value of the Grand Trunk Railway System, but the value of the group of railways of which the Grand Trunk Railway is but one, and how could we go into these questions? It would be a pure guess, not based upon any accurate knowledge.

In the case of the United States vs. the Boston Cape Cod and New York Canal Company, decided by the Circuit Court of Appeal, First Circuit, Massachusetts, on February 16th, 1921, and reported in 71 Federal Reporter (June 16th, 1921) elaborate reasons are given. A petition had been filed on behalf of the United States for condemnation against the Boston, Cape Cod and New York Canal Company, and this was an appeal on behalf of the United States from the judgment of Judge Morton. In this case it must be borne in mind that under the statute the actual cash value of the canal had to be appraised. Evidence had been given by a Professor Johnson as to the probable future revenue based on an increase of the tolls.

The Court at page 886 used the following language:—

"Then, again, the tolls which the Canal Company could charge on the interstate traffic passing through the Canal were subject to Governmental regulations and the opinion of Professor Johnson as to the probable future revenue based on an increase of tolls was in any aspect nothing more than a mere guess."

This case is also of value in dealing with the roseate views expressed by counsel for the Grand Trunk as to the future. In the head note on page 877 under Section 3, Evidence, it is said:—

"Future earnings of canal not proper subject of opinion evidence.

"In a suit by the United States for condemnation of a canal used for interstate traffic, the probable future tonnage of the canal and the additional revenue to be derived in view of such increased tonnage, held not a proper subject for opinion evidence."

And in the Reasons for Judgment the following language is used on page 886:—

“Tested by this rule, was the opinion of Professor Johnson as to the probable future tonnage of the Canal and the additional revenue to be derived in view of such increased tonnage a proper subject of opinion evidence? We think it was not. It seems to us that the jury might well be supposed to be able to determine the future increased tonnage of the Canal from a statement of the facts upon which the witness might found his own opinion. In this case it could be shown what the tonnage passing through the Canal was at the time of the taking, and the increase in the tonnage that had taken place from the time the Canal was opened to the time of taking. It could also be shown what the tonnage going around the Cape was at the time of taking, and what the increase was over a reasonable period antedating that time, and, from this and other competent evidence bearing on the question, we think the jury could form a correct judgment of the probable future increase on the tonnage through the Canal without the opinion of an expert.”

I agree with Mr. Lafleur's statement of the law laid down in the Cedar Rapids case, 1914 Appeal Cases p. 576 (p. 7036 of the Record): “For the present purpose it may be sufficient to state two brief propositions: First, the value to be paid for is the value to the owner as it existed at the time of the taking; not the value of the taker. Second, the value to the owner consists in all the advantages which the land possesses, present or future, but it is the present value alone of such advantages that falls to be determined. Where therefore the element of value over and above the bare value of the ground itself, commonly spoken of as the ‘agricultural’ value, consists in the adaptability for a certain undertaking—although ‘adaptability’ is really a rather unfortunate expression, the value is not a proportionate part of the assumed value of the whole undertaking.”

It is the present value alone of such advantages as falls to be determined. The stocks are acquired as of May, 1920. The value must be ascertained as of that date. The potential value would be reflected—to use a happy expression of Sir Thomas White—in the value as of May, 1920.

In the case of land, with a market value ascertained, the potential value would form part of the market value, and no difficulty arises. In the case of these stocks, there is no market value. If we were to look ahead—which I do not think would be proper—it will be seen that notwithstanding the increased rates for a portion of the year there was a deficit of earnings, outstanding, of about \$11,000,000 in 1920. It is argued that working expenditure would be lessened. If so, the rates allowed will likely be lowered. It is impossible to forecast what may take place. In dealing with the questions of potential value certain facts must be carefully kept in mind.

The value of these four classes of stock has to be ascertained as of the month of May, 1920, the date of the appointment of the Committee of Management.

Any potential value that can be attributed to these stocks must be ascertained as if the Government had not come to the relief of the railway. After the Government entered into the agreement and the Committee of Management was appointed the policy of the management altered; opposition of competing lines would cease, etc.

If therefore the value of these four classes of stock, including their potential value, is to be ascertained on the basis of the Grand Trunk System continuing to operate as theretofore, could any sane business man with a knowledge of the facts, come to any conclusion different from that come to by Mr. Chamberlin that a crash was inevitable, and insolvency and receivership the sequel, and would there be any reasonable chance of these four classes of stockholders ever receiving a cent on their investments? I think not.

By the agreement in question of the 8th of March, 1920, what the Grand Trunk Railway Company of Canada were agreeing to convey, and what His Majesty the King was purchasing, was the entire System, necessarily as a going concern. The

Crown has assumed obligations amounting to a very large sum of money. The earning of a sufficient amount to pay the interest on, and subsequently the principal of these obligations, depends upon the continued operation of the System as a going concern.

The schedule set out in detail the various properties comprising this System.

The first clause of the Agreement reads as follows:—

“1. Statement of Control.—The Grand Trunk represents that the companies, properties and interests comprised in the Grand Trunk Railway System are correctly and fully set forth in the first schedule to this Agreement, and that it has in such schedule correctly and fully shown how the various companies and their undertakings are controlled by the Grand Trunk, whether by stock ownership and to what extent, and whether by leases, agreements or otherwise, distinguishing in these the direct ownership and control by the Grand Trunk from the indirect ownership and control through companies included in the System.”

Clause 4 provides for the appointment of the Committee of Management of the Grand Trunk System.

Clause 10, headed, “Undisclosed Liabilities” is also important in this connection.

Clause 17 as to the “Superannuation and Pension Funds” is also important, indicating a continued operation of the System.

To my mind it is impossible to reasonably contend that “reconstruction value” can have any bearing on the matters to be determined by the Board. At the time of the Agreement all the properties mentioned in the schedules formed part of and were operated as a part of the System, and were passed to the Crown as an operating System, and no part of these properties has been severed from the System or any attempt made to sell them separately. If hereafter the Crown adopts the view that certain properties might be disassociated from the System and sold, and the assent of those having charges, and the necessary authority obtained, it is something these shareholders have no concern with.

I have given the best consideration I am capable of giving to the important questions submitted for our consideration and am of the opinion that our Award should be that there is no value in any of the four classes of stocks.

If equitable or moral considerations are to be considered, those who control the public funds must deal with the question, not the Board.

REASONS FOR AWARD

(BY THE RT. HON. SIR THOMAS WHITE, K.C.M.G., P.C.)

In the matter of the Arbitration under the Agreement dated the eighth day of March, 1920, between His Majesty the King and the Grand Trunk Railway Company of Canada, confirmed by Act of Parliament, Chapter 13, 10-11, George V.

The reference to arbitration herein arises under and by virtue of an Agreement dated the eighth day of March, 1920, between the Government of Canada (hereinafter called “the Government”) and the Grand Trunk Railway Company of Canada (hereinafter called “the Grand Trunk”), ratified and confirmed by an Act of the Parliament of Canada assented to on the eleventh day of May, 1920.

The purpose of the Agreement was to provide for the acquisition by the Government, upon the terms set out in the Agreement, of the “entire capital stock of the Grand Trunk except the four per cent guaranteed stock of the Grand Trunk amounting to £12,500,000.” As part consideration for such acquisition the Government agreed to guarantee the payment of:—

(a) Dividends payable half yearly at four per cent per annum upon the said four per cent guaranteed stock;

(b) The interest upon outstanding debenture stock of the Grand Trunk as and when payable in accordance with the terms thereof, consisting, as stated in the Agreement, of the following:—

Five per cent Grand Trunk debenture stocks.. . . .	£ 4,270,375
Five per cent Great Western debenture stocks.. . . .	2,723,080
Four per cent Grand Trunk debenture stocks.. . . .	24,624,455
Four per cent Northern debenture stocks.. . . .	308,215
Total.. . . .	<u>£31,926,125</u>

It was provided that the above-mentioned guarantees should be signed on behalf of the Government, and, forthwith, after the appointment of the Committee of Management referred to in the Agreement, should be deposited with the High Commissioner for Canada in London, England, "for the benefit and information of all parties concerned," and that concurrently with the deposit of the guarantees the voting powers at meetings of shareholders of the Grand Trunk, vested in or exercisable by the holders of the guaranteed stock and the debenture stocks, should cease and determine absolutely. The Committee of Management was formed on May 21, 1920.

The capital stock (other than the guaranteed stock) which was to be acquired by the Government (and is hereinafter referred to as the preference and common stock) is described in the Agreement as follows:—

First preference stock, five per cent.. . . .	£ 3,420,000
Second preference stock, five per cent.. . . .	2,530,000
Third preference stock, four per cent.. . . .	7,168,055
Ordinary or common stock.. . . .	23,955,437
	<u>£37,073,492</u>

With reference to the price to be paid by the Government for these stocks, the Agreement expressly provides:—

"The value, if any, to the holders thereof of the preference and common stock shall be determined by a Board of three arbitrators."

By section 11 of the Agreement a maximum limit is placed upon the amount which may be determined by the arbitrators as the value of these stocks. It is expressly stipulated that the fixing of this limit shall not be taken by the arbitrators as "any admission or indication that the value to be determined is the amount so fixed or any other amount."

Upon the value of the preference and common stock being finally determined, provision is made for payment to the holders thereof through an issue to them of non-voting four per cent fully paid capital stock of the Grand Trunk, upon which payment of dividends at the rate of four per cent per annum, payable half-yearly from the date of the appointment of the Committee of Management above referred to, is to be guaranteed by the Government.

Sections 12 and 13 of the Agreement set forth particulars as to this new guaranteed stock, its distribution to the holders of the preference and common stock which is being acquired by the Government, and as to the transfer of the said preference and common stock to the Government.

From the foregoing it would appear that the date as of which the value of the preference and common stock should be determined was the date of the appointment of the Committee of Management. Counsel for the parties were in accord as to this. The question to be determined is, therefore, "the value of the preference and common stock" to the holders thereof as of May, 1920.

It is to be observed that not all the capital stock of the Grand Trunk is the subject of the submission to arbitration. The £12,500,000 of "guaranteed" stock is not included. Furthermore, the existing debenture stocks aggregating £31,926,125 possessed certain voting powers which, with those pertaining to the guaranteed stock, have ceased and determined since the deposit of the guarantees of the Government in respect of these stocks.

The various subsidiary companies controlled by the Grand Trunk through stock ownership or lease, and also those companies controlled in turn by such subsidiaries, are set out in the first schedule of the Agreement. There are more than seventy in all of these companies which, with the parent Company, the Grand Trunk Railway Company of Canada, are designated in the Agreement as the Grand Trunk System. In presenting its case before the Board, counsel for the Grand Trunk used the expression "Grand Trunk System" as not including the Grand Trunk Pacific Railway Company and its subsidiaries and the Central Vermont Railway Company and its subsidiaries. They did, however, submit evidence as to the condition, earnings, and prospects of both these Companies and their subsidiaries. With respect to the entire System (as designated in the Agreement, including the Grand Trunk Pacific and Central Vermont Railway Companies and their subsidiaries), there was presented evidence covering in great detail and particularity its extent, alleged advantages and defects, condition of road-bed, terminals, plant, equipment and rolling stock and other property, its past, present and estimated future revenues and expenditures, its fixed charges, and the indirect or contingent liability of the Grand Trunk in respect of its guarantees of securities of the Grand Trunk Pacific and Central Vermont Railway Companies. The volume and character of business transacted, the outlook for future business, present and prospective rates and earnings were all made the subject of exhaustive evidence and argument before the Board.

With regard to the Grand Trunk Pacific Railway Company, all of whose issued capital stock is held by the Grand Trunk, counsel for the latter took the position that, as the stock was fully paid, the Grand Trunk was liable in respect of the Grand Trunk Pacific Railway Company (and its subsidiaries) only to the extent of its guarantees of that Company's bonds and debentures as that liability might appear, and subject, of course, to the ability of the Grand Trunk Pacific to meet its obligations in respect thereof. This appears to me to be the strictly legal view of the situation as between these two Companies, and I have adopted it as correct for the purposes of this finding.

As to the Central Vermont Railway Company and its subsidiaries, counsel for the Grand Trunk urged that deficits in the operation of these should not be taken into account in estimating the value of the stock of the Grand Trunk. The reason put forward in support of this contention is the fact that the Grand Trunk owns only seventy per cent of the stock of the Central Vermont Railway Company, which is a corporation separate and distinct from the Grand Trunk. As opposed to this view, it was contended that as important traffic originates upon the Central Vermont Railway, and as it has been operated as part of the Grand Trunk System, the financial results of such operation should be included in the accounts of the system for the purposes of evidence as to net earnings which should be taken into consideration by the arbitrators.

During the proceedings exception was taken by counsel for the Government to certain classes of evidence tendered by the Grand Trunk counsel, and judgment upon the points in issue was given by the Board. This may now be briefly referred to. The first exception taken related to evidence tendered as to the cost of locomotives owned by the Grand Trunk and employed in the operation of its system. The question of the admissibility of this evidence necessarily raised the larger question as to the admissibility of evidence as to the reproduction or replacement cost, or so-called physical value, of the right-of-way, terminals, rolling stock,

and other tangible property exclusively used for railway purposes. The judgment of the Board as to the question of evidence involved was rendered on February 7, 1921, a majority holding that for the purposes of this inquiry evidence as to reproduction or replacement cost, or so-called physical value, was valueless for the purpose of ascertaining the value of the preference and common stock of the Grand Trunk and therefore inadmissible. By the same judgments it was declared that the essential fact to be ascertained was the earning power, actual and potential, of the system and that all evidence bearing upon this was relevant and useful. With reference to this decision it may be observed that it related to property needed for railway purposes, which it was agreed by counsel for both parties could not be sold piecemeal and which it was not suggested should be dealt with in any way save as part of a going railway undertaking. It was pointed out in the judgments of the majority of the Board that no connection could be established between such valuation of the railway property of the Grand Trunk System and traffic rates likely to be established in Canada or United States.

The principal cases cited in support of the objection of counsel for the Government to this class of evidence were:—

Great Central Railway Company

vs.

The Banbury Union

1909 Appeal Cases, page 78.

London County Council

vs.

London Street Tramways Company

2 Queen's Bench Division L.R. 1894, page 189 et seq.

Dewsbury and Heckmondwike Waterworks Board

vs.

Assessment Committee of Penistone Union

16 Queen's Bench Division, page 596.

Since the judgments of February 7 were delivered a decision has been rendered in the Appellate Division of the Supreme Court of Ontario which has a close bearing upon the point in issue. The case was that of The Cobourg and Grafton Road Company *vs.* The Province of Ontario. In this case the toll road in question was taken by the Government of Ontario under the compulsory powers conferred by the Provincial Highway Act, and the question was as to the compensation to be made to the owner of the road. The Ontario Railway and Municipal Board, in giving reasons for its award, which was based upon a capitalization of the earning capacity of the road, rejected the principle of replacement value. Following is a quotation from the opinion of the Board:—

“The value of the land forming the highway cannot be estimated on the basis of the value of adjoining lands, since its only possible use is as a highway and its only productive value as such arises from the fact that used as a highway certain revenues may be derived in the form of tolls. These observations apply in a greater or less degree to the other tangible property and works which go to constitute the road and which are enumerated in the claimants' summary, viz., cut and fill, ditching, culverts, bridges, road-bed, and toll gates.”

Against the award of the Ontario Railway and Municipal Board an appeal was taken by the claimant. While differing as to the rate of interest which should be employed in the capitalization of the earnings of the road, the principle of valuation adopted by the Board was affirmed by the Appellate Division of the Supreme Court of Ontario.

Later during the proceedings, counsel for the Grand Trunk tendered evidence as to the valuation of certain buildings. These included elevators, freight and passenger stations, and hotels. The character of the evidence sought to be adduced is shown by the following extract from page 3765 of the record:—

“Q. You have made, I believe, an appraisal and valuation of the buildings I have just mentioned?

“A. Yes, a complete survey of the quantities and valuation.

“Mr. LAFLEUR: I am tendering this evidence like the other evidence we have tendered as to valuation.

“The CHAIRMAN: If it is objected to there will be the same ruling.

“Mr. TILLEY: You have built it up on the basis of what it would cost to build to-day?

“A. As at January 1, 1920.

“Q. What it would cost to build as at January 1, 1920?

“A. Yes.

“Q. Actual cost?

“A. Actual cost.

“Mr. TILLEY: Then I object to the evidence.

“The CHAIRMAN: It is ruled out.

“Hon. Mr. TAFT: In order to avoid any trouble just note my dissent.

“Mr. LAFLEUR: I point out in regard to the Fort Garry Hotel, Winnipeg, and the Macdonald Hotel, Edmonton, that these two buildings belong to the Grand Trunk Pacific Development Company, and that the Grand Trunk has a claim of about \$11,000,000 against that Company for advances of various kinds. I do not know whether that will affect the view of the Board as to our right to show what is the value of the physical assets of the Grand Trunk Pacific Development Company.

“Mr. TILLEY: My submission is you are not proving the value of the assets of the Grand Trunk Pacific Development Company. If the witness will give evidence as to what the two hotels would sell for now in the market, and the suggestion is made that that is their highest value, then I would admit the evidence.”

Formal tender was subsequently made by counsel for the Grand Trunk of evidence of the reproduction cost of the physical assets of the subsidiary railway, tunnel, terminal, dock, telegraph, steamship, development and other companies.

The nature of the evidence thus tendered is indicated by the following extract from the testimony of Mr. Berry at page 3223 of the official report of the proceedings:—

“Mr. BUTLER: You used the expression in your testimony this morning ‘sales value’ and sometimes ‘selling value.’ By that did you mean the cost of production or the cost of reproduction less depreciation?

“A. I mean cost of reproduction.

“Q. Without considering depreciation?

“A. Without considering depreciation.

“Q. In your answers made to me just now I understood you to say that by ‘sales value’ as used in your testimony you mean the reproduction cost?

“A. That is what I would sell it for.

“Q. And that is the meaning you give to ‘sales value’ as used by you in your testimony?

“A. Yes.

All this evidence like that of similar character tendered earlier was ruled out as inadmissible. Personally, I am unable to see that it could be of any value in enabling the Board to come to a conclusion as to the question in issue, viz., the value of the preference and common stock of the Grand Trunk. It was not suggested by

counsel for the Grand Trunk that the System as it stands should be disintegrated and its assets or any of them now actually in use turned into cash, or that its late Directors had ever had such policy in contemplation. Presumably, the use to which the physical assets of the various companies comprised in the System have been put has been that which was deemed best in the interests of the shareholders. Aside from this, the cases cited above are, I think, authority for the statement that reproduction cost of any building, work, or undertaking is not evidence of real value which depends upon the actual and potential earning capacity of the thing valued; in other words, what can be made out of it by way of actual return. Reproduction cost of a building or work may be of value in some cases as showing the maximum beyond which value should not go, but it affords no guidance as to actual value.

In the case of unproductive assets such as the land grants of the Grand Trunk Pacific Railway Company, evidence was admitted of selling value. Testimony as to value of the coal properties of the System was also received.

With regard to the question of the relevancy of evidence as to reproduction cost whether of property which can be used exclusively for railway purposes or which although used in connection with the System may be sold for what it will fetch, I adopt as the best criterion for establishing value the language of Lord Lindley in the case of London County Council vs. London Street Tramways Company, 2 Queen's Bench Division L.R. 1894, at page 206:—

"Cost price is well known to be no real criterion of the value of an outlay on land. What the result of the outlay will fetch is often much more and often much less than the outlay which has produced it."

And from the Judgment of Lord Justice A. L. Smith at page 219:—

"There can be no doubt that in an ordinary case where an undertaking such as the present is to be sold and paid for, its present, that is its true value, is in practice arrived at by capitalizing its rental value. I should say that this is the true way of arriving at its present value."

Benefit to the preference and common shareholders of the Grand Trunk could come only through the declaration of dividends from net earnings or from the sale of the assets of their Company for a sum in excess of its liabilities. Any purchaser buying such assets would, as to price which he would be willing to pay, have regard to what he would be likely to make in the way of annual return from his purchase. From whatever angle the question is viewed net earnings, actual and potential, seem to be the essential factor to be determined.

As having some bearing upon the matter of the value of the shares to be valued, records of quotations and sales of the preference and common stock on the London Stock Exchange over a considerable period of years were placed in evidence. In this connection it is to be noted that the agreement expressly prohibits the Board from taking into consideration the fluctuation in the market prices or quotations of these stocks caused by the negotiation of the parties, the passing of the Act or the execution of the agreement. Aside from this provision, however, it does not appear to me that stock market quotations or sales of individual lots of shares are of value in endeavouring to determine the true value of the large body of stock which we are called upon to appraise. Counsel for both parties were agreed that the question is not as to the value to any individual holder of his shares but as to the value of the shares as a collective whole or aggregate. The case of *Peek vs. Derry*, 37 Chancery Division, cited by counsel for the Government, clearly lays down the principle that it is real and intrinsic, not stock market quotation or value, which should be taken into account. In view of the foregoing it appears to me that the question at issue is what is the real value of the preference and common shares and that this real value depends upon the present and future earning power of the company.

10 In seeking to ascertain the earning capacity of the Grand Trunk we should, I think, consider all evidence relating to the earnings of the company as of the period

of the acquisition of the shares (May, 1920), as well as the earnings since that date and down to the present time. So far as possible, endeavour should be made to estimate probable future earnings, and for this purpose the earnings of the Grand Trunk System in the past, and especially before the abnormal period of the war, may be specially considered. All evidence as to physical condition of the system and its proper maintenance, the advantages or disadvantages of the location of its lines, volume of business, traffic rates, operating costs, and fixed charges must be given its due weight in its bearing upon the question of earning capacity, and there must also be taken into account the contingent annual liability upon guarantees of the Grand Trunk in respect of securities of other companies.

With respect to the net earnings of the Grand Trunk System (as defined by counsel for the company) for the past ten years, evidence of a minute and elaborate character was presented to the Board on behalf of both parties. A matter very much in controversy was as to whether, in the accounts disclosed by the books of the system, adequate allowance had been made for annual maintenance and whether, in addition, reserves should not have been created against depreciation of buildings, rolling stock, and other equipment. These are, of course, very vital matters, because if proper allowance be not made for current maintenance requirements and for depreciation in the annual profit and loss accounts of the system the true earning power in any year is not disclosed.

It was clearly proven in the course of the inquiry that the reports of earnings shown in the annual statements to the shareholders and to the Railway Department for many years past were inaccurate and misleading. For the year 1913 the published earnings were considerably larger than those shown by the books themselves. Later, during the years 1915, 1916, and 1917, a substantial portion of the earnings was concealed by the creation of an "inside reserve" account. Subsequently, this account was availed of to show during subsequent years larger earnings than were actually made. It is not necessary to deal here with the motives which actuated this policy on the part of the Board of Directors. It will be sufficient to say that these motives were fully revealed in the evidence and that they were not directly connected with the purpose of creating adequate reserves against deferred maintenance or depreciation. To the extent that reserves were so created they are, of course, to be taken into account in estimating earnings of the years over which they were built up.

Numerous exhibits showing in tabulated detail the results of the operation of the Grand Trunk System since 1910 were placed in evidence on behalf of both parties during the hearings. Out of this mass of testimony there finally emerged a clear and concise statement (Exhibit 470) prepared from the books of the company by its auditor, Mr. McLaren, showing the actual operating results of the Grand Trunk Railway Company of Canada by years irrespective of "inside reserve" or other hidden accounts. I am dealing now with the results of operation of the system as defined and limited by counsel for the Grand Trunk and not inclusive of the Grand Trunk Pacific or Central Vermont systems. The final tables of earnings presented by Mr. McLaren, in his restatement of accounts should, I think, be taken as records correctly compiled from the books of the company. Their accuracy was not in fact disputed by the other accountants who gave testimony before the Board. The accounts of the Grand Trunk System as restated by Mr. McLaren show the following annual results after payment of all operating expenses and fixed charges:—

Year	Surplus
1910..	\$ 3,617,876
1911..	4,188,783
1912..	4,482,448
1913..	2,874,592
1914..	2,014,176
1915..	5,755,730
1916..	11,319,341
1917..	3,402,540
1918..	3,872,344 Deficit
1919..	6,488,918 Deficit

To these figures must be added the following sums representing profits of subsidiary companies not taken into the accounts of the parent company:—

Year	
1910..	\$ 83,360
1911..	267,865
1912..	249,196
1913..	484,648
1914..	71,132
1915..	245,924
1916..	732,834
1917..	270,540
1918..	492,588
1919..	166,932

The deficit for 1920 exceeded six and a half million dollars. Including "Federal control" accounts it exceeded ten million dollars.

The restated accounts of the Grand Trunk Pacific and Central Vermont Railway systems which are not included in the above statement show in the aggregate exceedingly heavy deficits for the period in question. I shall refer to them more particularly later on.

From the foregoing it will appear that down to December 31st, 1917, the Grand Trunk System, according to its books of account, was making profits of varying amounts annually available for dividends, while from the end of 1917 down to December, 1920, very heavy annual deficits were incurred. Notwithstanding the increases in traffic rates which were authorized last autumn, the returns for the present year disclose a heavy deficit. The evidence of Mr. McLaren, Auditor of the Grand Trunk, shows the net results of the operation of the system (as defined by Grand Trunk counsel) for the period from January 1st, 1920, to the end of April, 1921. The net loss for this period was over five million dollars. As against the increased traffic rates to which reference has been made, the higher wage scale which went into effect early last year, and the decrease in traffic owing to trade depression following the war, have proven more than an offset.

MAINTENANCE

A question very much in controversy during the proceedings was as to whether the Grand Trunk management had made from year to year proper provision for maintenance of way, structures, equipment, and plant. Counsel for Grand Trunk contended that with the exception of the latter years of the war period, when labour and material were difficult to obtain and during which reserves against deferred maintenance were built up, the System had been maintained to the extent necessary for maximum operating efficiency. Against this view counsel for the Government claimed that for a long period of years the System had been steadily deteriorating by reason of failure to provide out of annual earnings for adequate maintenance and depreciation of equipment and other property, and that in consequence of such failure the actual net earnings of the Company in years for which profits were shown were materially less while the deficits for years of loss in operation were in reality greater than appeared from the books of the Company.

The evidence adduced on this point conclusively established, in my judgment, the essential soundness of the contentions in this regard of the Government.

It was admitted by the Grand Trunk counsel that no special fund had been created against depreciation of rolling stock, buildings, plant, and other equipment of the Canadian part of the System. By Canadian railway law no such fund is required to be maintained. With respect to the American lines forming part of the System, adequate provision against depreciation is required to be made and the Grand Trunk has observed this requirement in the accounts of its subsidiary railway companies operating in the United States. Aside from legal requirements, it seems clear that net earnings cannot be accurately determined for any year without setting aside such a sum as in accordance with the practice of well-managed railway systems will

serve as a setoff against the year's depreciation. The authorities are quite clear as to this. See Bryce on "Ultra Vires," 3rd edition, at page 340, as to the meaning of "profits"; also the statement of Jessel, M.R., in *Davison vs. Gillies*, 16 Chancery Division 344.

What amount should have been set aside yearly for depreciation the evidence does not help us to determine. It is clear, however, that a considerable annual provision in this respect should have been made in respect of the Canadian portion of the Grand Trunk System before net earnings were assumed to have been made.

With regard to annual maintenance the evidence showed a much more serious state of affairs. The System, at the time of its taking over by the Committee of Management in May, 1920, was confronted with an exceedingly heavy programme of expenditure for deferred maintenance and capital construction. During the last two years of the war a good deal of work of this character had been suspended, but in my view of the evidence a considerable part represented maintenance and construction which should have been done in the pre-war and early war period; in fact, the System over the past ten years and longer does not appear to have been adequately maintained, with the result of gradual deterioration in physical condition and increasing accumulation of deferred maintenance requirements. During the year 1920, after the Committee of Management was appointed, very heavy expenditures were made with the purpose of overtaking work of this character, with the result that the greater part of the System was put in a condition suitable for operating efficiency. Exhibit 457 shows that for the years 1911 to 1917 inclusive an average sum of about six million dollars per annum was expended for maintenance of ways and structures. For 1918 the expenditure under this heading was \$11,600,000, for 1919, \$17,000,000, and for 1920, \$18,100,000. Making due allowance for increased costs of materials and wages, these figures indicate the extent to which maintenance had become deferred. The finding with respect to the matter of annual maintenance must, I think, be that inadequate provision was made for it during a long period of years past and that consequently the net operating earnings of the Company as shown by its books did not truly reflect the real condition of affairs. The letter of Mr. Kelley, the Chief Engineer and new President of the Company, dated March 5, 1917, shows clearly the very serious condition of the System with respect to the matter of deferred maintenance, which he estimated at over \$21,000,000. The so-called "inside reserves" created by the Company prior to this date were quite inadequate to meet the deferred maintenance requirements of that period.

After all the heavy expenditure made upon the System from its taking over in May, 1920, until the end of that year, deferred maintenance to the amount of many millions still remained to be done in respect of bridges, trestles, culverts, crossings, ties, track, rails, ballast, track-laying and surfacing, fences, docks, and wharves. Evidence adduced by the Government shows estimated extraordinary maintenance and capital requirements in respect of the Grand Trunk System for the years 1921-1925 inclusive as follows:—

Extraordinary maintenance.. . . .	\$ 8,924,318
Remunerative capital.. . . .	4,780,087
Non-remunerative capital.. . . .	43,908,612
Total capital.. . . .	48,688,699
Total capital and maintenance.. . . .	57,613,017

The estimate for 1920-1925 according to testimony on the part of the Government was as follows:—

Extraordinary and deferred maintenance.. . . .	\$18,889,343
Remunerative capital.. . . .	6,887,184
Non-remunerative capital.. . . .	43,908,612
Total capital.. . . .	50,795,796
Total capital and maintenance.. . . .	69,685,139

A large part of the item for non-remunerative capital consists of estimated expenditures for grade separations in Montreal, Toronto, Detroit, Chicago, and other

cities, which must be carried out in the not-distant future. Making the most liberal allowance for all that was adduced against these figures, it is clear that the expenditures with which the Grand Trunk was confronted in May of 1920 for deferred maintenance and capital construction were of most serious amount and of the gravest financial consequence. Mr. Kelley's letter referred to above indicated necessary capital expenditure (over and above deferred maintenance) of an amount exceeding thirty million dollars, the principal item being for rolling stock and shop machinery. The above figures as to deferred maintenance and capital expenditures relate only to the Grand Trunk System exclusive of the Central Vermont and Grand Trunk Pacific systems. The condition of the former as to these items was shown to be quite serious as to deferred maintenance, while that of the Grand Trunk Pacific was of the gravest character.

With respect to the revenues of the Grand Trunk as shown in its accounts, it was proven in cross-examination that large sums were included representing charges for interest upon advances or loans made to certain of its subsidiaries. Some of these advances are quite large, as for example ten million dollars to the Grand Trunk Pacific Development Company and eleven millions to the Grand Trunk Pacific Branch Lines Company. It is clear from the evidence that some of these charges aggregating very large amounts do not represent collectible indebtedness. In so far as such uncollectible indebtedness entered into the accounts of the company as part of its revenues, the annual statements of net earnings were inaccurate and misleading.

In view of the foregoing, it is plain that without taking into account the contingent liability of the Grand Trunk Railway Company of Canada in respect to securities of the Grand Trunk Pacific Railway Company the financial position of the former was most precarious at the time of the appointment of the Committee of Management in May, 1920, which is the date as of which the preference and common shares are to be valued. The years 1918, 1919, and 1920 show deficits of \$3,872,344, \$6,488,918, and \$6,719,362 respectively. The results for the year 1921 show to date a like heavy deficit. Deferred maintenance requirements were large and pressing. In addition, there was confronting the company the program of extraordinary maintenance and capital construction to which reference has been made. Exhibit 474 filed by counsel for the Government shows estimated net cash requirements of the Grand Trunk System for the fifteen months ended March 31, 1922, to be nearly ninety million dollars. Whether, in the financial conditions prevailing in 1920 and since, the company, even if had been relieved of its obligations in respect of the Grand Trunk Pacific, could have met its own situation unassisted by Government aid in the way of direct loans or guarantee of its securities, can only be made the subject of conjecture. My view upon the evidence is that the credit of the company would have proven unequal to the emergency and that a receivership would have been inevitable if not in 1920 then in the next year or two. I do not believe that with such yearly deficits the company could have long continued to float its securities to the amount necessary to meet them and to provide for its heavy program of deferred maintenance and capital requirements. This much, however, is clear. There would have been no dividends available for shareholders in 1920, 1921, nor, so far as can be seen, for many years to come. When to this situation is added the burden of the Grand Trunk's guaranteed liability in respect of the Grand Trunk Pacific Railway Company it will be clear how impossible it would have been for the Grand Trunk Railway Company of Canada to continue as a solvent going concern. The extent of this contingent liability is shown by Exhibit 319 as follows:—

	Principal	Annual interest
Guarantee on funded debt..	\$54,889,000	\$2,292,760
Contingent guarantee of interest on 4 per cent debenture stock..	1,395,170
Total..		\$3,687,930

The Grand Trunk is liable upon its guarantee of both principal and interest of the funded debt. Its guarantee of the payment of interest upon the 4 per cent debenture stock is out of net earnings of the Grand Trunk in each year after deducting working expenses and certain interest charges. If, in any year after payment of such working expenses and other charges, any net earnings remain over, the liability of the Grand Trunk upon such guarantee for the year in question would have to be met in priority to any dividend distribution. The statements presented to the Board show clearly the grave financial condition of the Grand Trunk Pacific Railway now in liquidation. This company is hopelessly bankrupt with no prospect now or for years to come of earning even its operating expenses, much less its fixed charges. The contingent liability of the Grand Trunk in respect of the securities mentioned must be regarded as a continuing charge against the earnings and credit of the Grand Trunk until full payment is made in accordance with the terms of the guarantees. It is quite clear that nothing by way of relief can come from the earnings of the Grand Trunk Pacific Railway undertaking. The liability thus imposed upon the Grand Trunk is so serious that it is desirable to carefully describe and analyze the condition and prospects of this company in order to show the facts upon which these conclusions are founded. It would be difficult to imagine a more misconceived project than that to which the Grand Trunk committed its credit in this unfortunate enterprise. For nearly half the distance of nine hundred miles westward from Winnipeg the main line was constructed close to and between the lines of the Canadian Pacific and Canadian Northern Railway Companies. For the remaining thousand miles to Prince Rupert the main line traverses for the most part a difficult country, largely mountainous, whose development for the purpose of furnishing local traffic must await settlement and business enterprise, and terminates at Prince Rupert, a port as yet without any considerable trans-Pacific or other external trade. For two hundred miles or more this section of the main line parallels the line of the Canadian Northern Railway Company so closely that part of the rails of each has been taken up and both railways, now under Government control, use the same tracks. When it is considered that the Grand Trunk Pacific was built for the whole distance of eighteen hundred miles from Winnipeg to Prince Rupert at a very high standard of construction and at enormous cost, particularly in the mountain section, the magnitude of the mistake in going forward with this enterprise is apparent. The branch lines in the Prairie Provinces are wholly inadequate as feeders to the main line, providing a strikingly unfavourable contrast to the number and mileage of the branch lines of both the Canadian Pacific and Canadian Northern Railway Companies in this great traffic-producing area. Part of the Grand Trunk Pacific branch line system is badly situated in territory tributary to its rivals. As a result of the location of its main line and its want of efficient feeders, the Grand Trunk Pacific Railway Company will not share proportionately with its rivals in the traffic which may be expected with the progressive settlement and development of the Prairie Provinces. As to the lease of the Eastern Division of the National Transcontinental Railway which the Grand Trunk Pacific Company was to take after the completion of the Division, I eliminate it from consideration. It was never executed, and as the Government has been operating the Eastern Division the agreement providing for the lease may be regarded as having lapsed and as not imposing further liability upon the Grand Trunk Pacific Railway Company. The financial position of this company since its system was declared open for operation at the close of 1915 may be briefly shown as follows:—

Year	Deficits
1916.. . . .	\$ 1,358,435
1917.. . . .	5,300,512
1918.. . . .	6,318,594
1919.. . . .	11,940,032
1920.. . . .	23,141,016

These are the deficits after taking into account operating expenses and fixed charges. They with the other evidence as to financial condition show conclusively that the company is bankrupt and that Receivership was unavoidable.

From this it will be seen that the company is quite incapable of meeting its liability upon its issued securities guaranteed by the Grand Trunk Railway Company of Canada. It should be further pointed out that the above figures which are compiled from the books of the company cannot be regarded as accurately reflecting the earnings of the company because of the failure to provide any reserves against maintenance or depreciation. The maintenance charges with which the Grand Trunk Pacific will be confronted during the next ten years will be exceedingly heavy reflecting as they must the wear and tear of the last five years of operation, during which, as construction was recent, the amount of expenditure for maintenance was small. The evidence shows that about twenty million dollars is now required to meet deferred and extraordinary maintenance.

It would be difficult to overstate the serious character of the obligation imposed upon the Grand Trunk by the failure of the Grand Trunk Pacific enterprise to realize the hopes built upon it at its inception. It is quite clear that, whether the war had occurred or not, it would have been utterly impossible for the Grand Trunk to carry the burden of its liability in respect of guarantees upon Grand Trunk Pacific securities. A glance at the earnings of the Grand Trunk for the past ten years makes this evident. That the position was fully understood and appreciated by the management of the Grand Trunk is shown by the letter of the Chairman of the Board, Sir Alfred Smithers, in December, 1915, to Sir Robert Borden, Prime Minister of Canada. The Grand Trunk Pacific Railway undertaking was then about to be taken out of its construction stage. The Chairman in this letter pointed out the situation with which the Grand Trunk would be immediately confronted, and suggested as the only solution that the Government should take over the Grand Trunk Pacific System as from January 1, 1916, relieving the Grand Trunk of all its liabilities in respect thereof and repaying to the Grand Trunk all advances made to the Grand Trunk Pacific Railway Company, the Grand Trunk Pacific Development Company, and its subsidiary companies. Referring to these liabilities, Sir Alfred says: "Under present circumstances it is quite impossible for the Grand Trunk Railway Company to meet the extra liabilities arising from the Grand Trunk Pacific Railway Company." And again: "We have done our utmost to meet the heavy financing which has been necessary and the difficulty of which has been immensely increased by the disastrous war conditions. We are now 'at the end of our tether' with regard to Grand Trunk Pacific financing." The letter of Mr. Chamberlin, President of the Grand Trunk, addressed to the Commission appointed in 1916 to examine into and report upon the Canadian railway situation, is even stronger in its statement of the gravity of the Grand Trunk's position. This letter is dated January 30, 1917, and is filed as Exhibit 458. To the question as to the effect on the Grand Trunk should the operation of the Grand Trunk Pacific be left as it was and the former not relieved from its guarantees, Mr. Chamberlin said: "There can be only one answer; it would mean a Receivership for the Grand Trunk Company carrying with it the destruction of its credit for some time to come and the impairment of the credit of the Dominion."

No other view can, I think, be reasonably taken upon the evidence presented to the Board than that in May, 1920, had the agreement providing for the acquisition of the preference and common shares of the Grand Trunk and for financial assistance by the Government not been entered into, the Grand Trunk Railway Company of Canada, struggling with its own deficits and requirements for deferred maintenance and capital construction and burdened with its heavy annual liabilities in respect of Grand Trunk Pacific securities, must inevitably have gone into Receivership.

During the course of the proceedings it was suggested to the Board by counsel for the Grand Trunk that the Grand Trunk had serious cause for complaint against

the Government of Canada in respect of the Grand Trunk Pacific undertaking. Particularly was it urged that the Grand Trunk in 1903 desired to build its western system from North Bay (in Northern Ontario) and acted only from compulsion in proceeding with the National Transcontinental project. It was also complained that after the inauguration of the Grand Trunk Pacific undertaking the Government permitted rival railway companies to construct lines in territory which it traversed. The evidence before the Board disclosed no ground for such complaints. No doubt both the Government of the day and the Grand Trunk authorities were gravely mistaken in 1903 as to the cost and future possibilities of the Transcontinental Railway enterprise. But the Grand Trunk was not obligated to proceed with it. The Agreement providing for the construction and financing of the project was entered into by the Grand Trunk acting under no compulsion. The Grand Trunk Railway Company of Canada was the sole holder of the stock of the Grand Trunk Pacific Railway Company. * Any profits from the enterprise would have come into its treasury for the benefit of its shareholders. That high expectations were entertained as to the advantage to be derived by the Grand Trunk from the construction of the National Transcontinental Railway as authorized by Parliament is clear from the optimistic speeches made by the President and General Manager at the meeting of shareholders in 1904, when authorization was given to pledge the credit of the Grand Trunk to the obligations devolving upon it under the Agreement. The evidence shows that the Government not only carried out its financial part of the bargain but during a long course of years afterwards—in fact until the Receivership in 1918—made loans aggregating more than fifty million dollars to the Grand Trunk Pacific Railway Company for the purpose of enabling it to complete its construction and pay its annual deficits. The Agreement for the construction of the Grand Trunk Pacific Railway has been an unfortunate one both for the Government and the Grand Trunk, but it was nevertheless an agreement deliberately entered into by the Grand Trunk in the expectation of gain from a successful project. For the charge that the Government unfairly permitted rival companies to build into territory traversed by the Grand Trunk Pacific there appears not the slightest foundation. On the contrary, the evidence clearly shows that the Grand Trunk Pacific enterprise was launched into territory in the Prairie Provinces already occupied and in process of occupation by the Canadian Pacific and the Canadian Northern Systems, and that, before the Grand Trunk Pacific enterprise was entered upon, express notice in writing had been given to the Grand Trunk by the Canadian Northern Railway Company that it possessed the necessary charter powers and intended to extend its system easterly through Ontario and Quebec and westerly to the Pacific ocean. The Agreement providing for the construction of the Grand Trunk Pacific railway contained no covenant on the part of the Government that no new construction would be authorized by Parliament in the territory traversed by the Grand Trunk Pacific Railway enterprise.

I mention these matters because they appear to have been put forward as raising some equitable claim in favour of the Grand Trunk. It is clear, however, that as no legal claim is involved complaints of this character could not be taken into consideration in these proceedings. The agreement for the construction of the Grand Trunk Pacific undertaking was entered into, the financing therein provided for was carried out, the obligations of the Grand Trunk by way of guarantee upon the securities of the Grand Trunk Pacific Railway Company were incurred and are in effect, and the sole question before the Board is as to the value of the preference and common stock of the Grand Trunk, having regard to all relevant factors, including these obligations, as of May, 1920.

During the course of argument it was suggested by counsel for the Grand Trunk that a sale of the undertaking of the Grand Trunk Pacific might result in a surplus available in relief of the Grand Trunk in respect of its guarantees. It is clear upon the evidence that the result of no sale, judicial or otherwise, would suffice to produce a sum equal to the charges which have priority over the securities so guaranteed.

The guarantees will have to be met according to their terms without hope of abatement from earnings or sale of the Grand Trunk Pacific enterprise.

Apart from its guarantees upon Grand Trunk Pacific securities, the evidence shows that the Grand Trunk is liable upon a guarantee of interest on 4 per cent bonds of the Central Vermont Railway Company to an amount of \$13,359,000. Considering the unsatisfactory earnings of the Central Vermont system and its past history, it is impossible to say that no loss will be incurred by the Grand Trunk in respect of this of this guarantee. I do not, however, in this finding, treat this obligation as one upon which loss will be incurred.

Reviewing all the evidence in the case I have reached the following conclusions:—

(1) The actual earning power of the Grand Trunk Railway Company of Canada before, during, and since the war, and, so far as can be estimated, for the future does not justify the assumption that any profits would, from the date of the acquisition by the Government of the preference and common shares, viz., May, 1920, ever have been available for distribution to the holders thereof, after providing for the contingent liability of the company in respect of Grand Trunk Pacific securities guaranteed by the company and dividends upon the "guaranteed stock."

(2) Having regard to its own continuing heavy deficits, the necessity for making provision for deferred and extraordinary maintenance and capital construction, and its heavy liabilities in respect of securities of the Grand Trunk Pacific Railway Company bearing its guarantee, the Grand Trunk Railway Company of Canada, but for the financial support of the Government since May, 1920, must have been forced into a receivership.

Upon these conclusions I find that the preference and common stock of the Grand Trunk Railway Company of Canada has no value. Any question as to compassionate consideration of the shareholders must be for the Government and Parliament of Canada to deal with and not for this Board.

REASONS FOR DISSENT

(BY THE HONOURABLE WILLIAM HOWARD TAFT)

This is a proceeding to determine the value of the First Preference five per cent (5%) stock of the Grand Trunk Railway Company of Canada, amounting in par value to £3,420,000; of the second preference five per cent (5%) stock, amounting to £2,530,000; and of the third preference four per cent (4%) stock, amounting in par value to £7,168,055, and of the common stock of the railway company, amounting in par value to £23,955,437. The proceeding is conducted in accordance with an agreement dated the 8th day of March, 1920, between the Government of Canada and the Grand Trunk Railway Company of Canada, authorized and embodied in enabling and confirming statutes of the Dominion Parliament. The object of the various Acts of Parliament and of the agreement is to transfer to the Government the control of the Grand Trunk Railway of Canada and all the subsidiary corporations over which it exercises control, by reason of ownership of the stock of such companies, or by lease. The names of the companies whose stock thus passes into the control of the Canadian Government are set forth in the agreement and the statute.

As part consideration for the acquisition of the control of the Grand Trunk Company, the Government guarantees the interest upon the present debenture stocks in accordance with their terms, which are as follows:—

Five per cent (5%) Grand Trunk debenture stock.. . . .	£ 4,270,375
Five per cent (5%) Great Western debenture stock.. . . .	2,723,080
Four per cent (4%) Grand Trunk debenture stock.. . . .	24,624,455
Four per cent (4%) Northern debenture stock.. . . .	308,215

Total.. . . . £31,926,125

In addition to this, the Government of Canada agrees to issue new stock of the Grand Trunk Company of a par value of £12,500,000 with a guaranty by the Govern-

ment of four per cent annual dividend thereon, in exchange for an existing issue of four per cent stock of the same par value, guaranteed by the Grand Trunk Company which is non-cumulative but prior in right to the preferred and common stock already described.

Under the statutes creating the Grand Trunk Railway Company, holders of the debenture stocks and the guaranteed stock had certain voting powers, which under the contract are to cease, so that the voting power is to vest solely in the three preference stocks and the common stock to be transferred.

The sixth and eighth clauses of chapter 13 of the 10-11 George V, providing for the present arbitration, are as follows:—

“6. *Submission to Arbitration.*—The value, if any, to the holders thereof, of the preference and common stock shall be determined by a Board of three arbitrators, one to be appointed by the Government, one by the Grand Trunk and the third shall be Sir Walter Cassels, Judge of the Exchequer Court of Canada, who shall be Chairman of the Board. Should Sir Walter Cassels die or be unable to act, the said parties shall agree upon another third arbitrator, who shall be either the then Judge of the Exchequer Court of Canada, or one of the Judges of the Supreme Court of Canada, and who shall likewise be Chairman. Should any vacancy occur in the Board of Arbitrators, other than the third arbitrator, the arbitrator to fill the vacancy shall be appointed in the same way as the arbitrator whose seat has become vacant was appointed.

“8. *Making of Award and Appeals.*—The award shall be made by the arbitrators, or a majority of them, within nine months from the appointment of the arbitrators, or within such further time as the Governor-in-Council may approve. The unanimous award of the arbitrators shall be final, but should the award not be unanimous, and should notice of appeal be given by either party to the other within thirty days after the making of the award, an appeal therefrom upon any question of law shall lie to the Supreme Court of Canada, and or to the Judicial Committee of the Privy Council, if leave be granted by the said committee.”

The Board has been constituted in accordance with Section 6. After convening in September and October, 1920, the members of the Board were taken over the main line of the Grand Trunk Railway Company from Montreal to Chicago. They then visited the Pacific Coast and viewed the Grand Trunk Pacific Railway, all of whose capital stock is the property of the Grand Trunk Railway, and control of which would therefore pass to the Government under the present proceeding by the acquisition of the Preferred and Common Stock of the Grand Trunk.

On the 1st of February, 1921, the evidence began, and for seventy-three days we had hearings, resulting in the submission of 8,000 typewritten pages of evidence and over 500 Exhibits. The question to be settled is of a class of questions the most difficult ever presented to a tribunal, to wit, to determine the fair value of a great railway System, with all its accessories and subsidiary companies for the purpose of purchase and sale. In substance, the Government of Canada is taking over the ownership and control of the whole Grand Trunk Railway System, including all its subsidiary railways and other corporations. The Government in effect agrees to assume,

First, the funded obligations of the Grand Trunk Railway of Canada,

Second, to issue four per cent absolute Government obligations of a par value of £12,500,000, with which to take up the present so-called Guaranteed capital stock of that amount which is prior in right of dividends to all other issues of capital stock, but is dependent on earning and non-cumulative, and

Third, to deliver in the same kind of four per cent obligations, to the owners of the subsequent three Preferred issues of stock and the Common Stock, whatever this Board within the maximum limit of \$64,166,666.66 shall determine the stock to be worth.

The Grand Trunk Railway Company was organized under a Canadian Charter in 1852. It was the pioneer railway of Canada. It was financed wholly by British capital, and its Board of Directors have always met in London, and there taken corporate action. The present shareholders are and always have been residents of the British Isles. The shares of stock have been placed upon the London Stock Exchange, and have been dealt in as a speculative stock. The stock was fully paid up in cash. The vicissitudes of the company have been such, however, that in 1860 the enterprise seemed likely to go to the wall, but with concessions made by then bondholders, new capital was secured, and the company set upon its feet again. It constructed or acquired, in the province of Ontario, a great many branch lines. Indeed it purchased competing lines, so that its mileage in that province is greater than that of any other railroad. It owns a line from Windsor, opposite Detroit, to Buffalo, and it has two parallel lines from Toronto to Sarnia. Its main line is a double track line from Montreal through Toronto and Hamilton to Sarnia on the St. Clair River, through a tunnel under that River to Port Huron, and thence to Chicago over the lines of the Grand Trunk Western Company of Michigan, of which the Grand Trunk Company owns all the stock. An important double track connection from Hamilton, on the main line between Sarnia and Toronto, to Suspension Bridge and Buffalo, makes a double track railway trunk line from Chicago east and from Montreal and Toronto south to the Niagara Frontier, whence by the Lehigh Valley, with which the Grand Trunk interchanges traffic, it reaches New York. From Montreal east the Grand Trunk has a line to Quebec, and by a line which the Grand Trunk, at the instance of, and with some pecuniary assistance of, the Canadian Government, built, it reaches Portland, Maine. From Montreal south by some of its subsidiaries, including the Vermont Central, it reaches White River Junction, whence through a connection with the Boston and Maine, it reaches Boston. By the same Central Vermont, it passes through Palmer, Massachusetts, and thence to New London, Connecticut, whence a boat line of the Company carries freight to New York. The Harbour at Portland is open the year round, while the harbours at Montreal and Quebec are closed during the winter season. The Grand Trunk, therefore, has a main trunk line from Chicago through Michigan and Canada to the sea at Montreal, at Quebec, at Portland, at Boston, and at New York, the latter by two routes. With its many branch lines in Ontario and in Michigan, the Grand Trunk connects its lines with the Great Lakes at many points, and operates partly water, partly rail routes from east to west. The Grand Trunk has complete or partial ownership of steamship companies, elevator companies, electric lines, subordinate railway lines, bridge companies, terminal companies, and other corporations owning hotel properties used in connection with the railway system.

The Grand Trunk System, as that term is understood in this case, includes the Grand Trunk Company of Canada, the Western lines, i.e., those of the Grand Trunk Western of Michigan, and the New England Lines, i.e., the lines to Portland. The Grand Trunk System does not include the Vermont Central, which, though largely owned by the Grand Trunk Railway Company of Canada, is run separately. Its accounts are kept separately.

In 1897 Mr. Charles M. Hays was called from the Wabash Railway System to become the President of the Grand Trunk Railway Company of Canada and the System. He found a railroad at that time which was not well equipped, and could not be considered more than a third-class transportation system. He found a property operated under a Charter which was so drawn as to emphasize the right of the stockholders to have dividends immediately declared out of the net earnings of the company at the end of the year, and was thought to vest no discretion in the Directors to hold the earnings for carrying out broad policies and enlargement of the usefulness and ultimate earning capacity of the company. It is quite evident, from the history before us, that Mr. Hays found it difficult to secure from the shareholders consent

to the acquisition of needed additional capital properly to equip and reconstruct the road and to enlarge its transportation capacity. It is further obvious that in his efforts to do this, he increased the operating expenses by including in them outlays in the matter especially of motive power, freight and passenger cars, which should have been properly charged to capital and regarded as a new investment, rather than as current additions to operating cost. In this way, he was enabled to improve the road materially and make it a first-class railroad, without calling upon the stockholders for great additional capital. He thus withheld from them dividends that possibly might have otherwise been declared. From the evidence of Mr. Williams, a very experienced expert in the management and development of railways, now the President of the Delaware and Hudson Canal Company, it is clear that the motive power and the car equipment of the Grand Trunk has been improved and maintained with a minimum charge to capital, and with a very large charge to revenues, and that in the years 1910, 1911, and 1912, the company had been gaining in its capacity for doing the business and in the efficiency of its equipment, and had taken on the character of a great trunk system.

I have been impressed by the number of skilled, loyal, reliable and most experienced employes, the heads of bureaus and departments, who have filled the general offices, and who have been in the employ of the Grand Trunk for many years—indeed, who entered the employ in their youth, and have continued loyal to the company until their maturity and old age. Through a school of apprentices and other methods, an esprit de corps has been acquired that has been very valuable to the company, and it can be stated with confidence that had the policy of the company, as dictated from London, been as prudent, as wise and as effective as the local management through the officers of the Grand Trunk here, the fate of the property would have been different.

The Grand Trunk System has been burdened with a very great number of branch lines, and with some lines parallel to its main trunk line, which it acquired to avoid competition, and which are not a source of profit. Many of the branch lines of course are feeders, but it is quite apparent that they are in some respects a burden. In a degree the same thing has been true of branch lines acquired in Michigan, but the marvellous growth of business in that State in the centres reached by the Grand Trunk is very likely to make them very profitable. With much care and wisdom the business of the Grand Trunk System has been nursed into a large through traffic between Chicago and the Atlantic Seaboard. While the amount of business done in the United States by the Western Lines and the New England Lines of the Grand Trunk System is not more than one-third of the Grand Trunk Railway of Canada, the business which has come to the Grand Trunk is perhaps 70 per cent due to its business from and to the United States, to and from Canada, and to other business from and to points in the United States through Canada to and from other points in the United States. This main line through business has been encouraged in every way and with much foresight and ability. The road has been maintained so that the immense burden which was thrust on the road during the war times was carried without a break. Of course, the volume of business was temporarily increased by war conditions. Nevertheless, the business of the Grand Trunk has shown a steady increase not alone in its operating revenues, which are often a misleading guide, due to increases in rates, but in its statistics of tons carried per mile.

Mr. Kelley, who is the very able President of the Grand Trunk System, and whose ability has been recognized by his continuance in the management of the road, after its transfer to the Government, testifies that the road is in good operating condition, and that it could, without substantial expense, meet a fifty per cent increase in its business.

One of the advantages which the Grand Trunk enjoys, and it is a real one, is the foresight with which land has been acquired in Chicago, in Detroit, in Toronto,

and in Montreal for enlarging the terminal facilities in those cities to meet the growth of business. Of course it will take capital outlay to equip them properly, but the land is there and conveniently situated for the purpose. On the other hand, the Grand Trunk is rather unfortunately situated in respect to grade separations in cities. It has a very valuable entrance to Detroit, and its right-of-way, though at places somewhat narrow, passes through the centre and business part of the city. It crosses a great many streets and there is likely to be a movement to require the Grand Trunk to elevate its tracks and separate its grades from that of the streets. This is a very expensive matter. It is, however, something that it takes a good deal of time to bring a railroad to do, but the railroad must gradually make preparation to meet the expense. There is a similar situation in Montreal. The Bonaventure station is an old structure, and while very conveniently situated in the city, does not offer very ample accommodations. There are many grade crossings in the approach to the station and an agitation has already begun looking to the separation. The company, in anticipation of the necessity, has expended a considerable sum in the purchase of land needed to widen its approaches to the new station. The city itself must contribute part of the amount to be expended and this fact will probably enable the company to postpone the separation for a number of years. In Toronto the case is more urgent and involves a new Union Station which has been built and for which the companies have entered into bond obligations. The station is erected with a view to the elevation of the tracks. The Grand Trunk has already elevated its tracks west of the station, but there is a great deal of work of a similar character to be done to the east, and \$4,000,000 has been spent in the new station. A burden of something like ten millions of dollars each threatens the Grand Trunk and the Canadian Pacific in the uncertain future. The entrance to Chicago is over the tracks of the Western Indiana in which the Grand Trunk owns a certain amount of stock. These are elevated. The Grand Trunk has a fractional interest, too, in the Chicago Belt Line, whose tracks are also elevated. But for several miles near the limits of the city, the tracks of the Grand Trunk have grade crossings which are in the uncertain future to be removed by separation, and the city authorities of Chicago are gradually pressing toward this consummation.

A subordinate engineer in charge of grade separations of the company, called by the Government, testified that the expenses of these grade separations, including those of London, Ontario, and South Bend, Indiana, would amount to some \$46,000,000. There is no likelihood that either at London, or South Bend, there will be any money spent for such a purpose till the company is quite ready, and yet \$13,500,000 are assumed to be needed for those in the next five years. This estimate on the part of this official was a personal one, had never been submitted to his superior officers, and is not one, I think, which we should take as serious. He had made no calculation or investigation as to how the Grand Trunk would be aided by the New York Central, the Canadian Northern and other roads who must in equity contribute and at least one of which has agreed to do so. This witness himself thought this work might be spread over 20 years. It would not be unreasonable to divide this estimate by two and lengthen the time in which the money would have to be spent.

The physical condition of the railroads in the United States was not improved by the war. The shortage of labour and the very high wages which had to be paid to the labour which could be secured, and its low efficiency, as well as the high cost of material, furnished strong motives for reducing the current maintenance to as low a point as possible, consistent with the safety of the road. Doubtless in this respect the Grand Trunk was no exception. In the restoration of normal conditions, it is natural that maintenance and capital expenditures that often accompany maintenance under such circumstances should be made, but railroads that are not rich will if they are wisely managed do this as gradually and economically as they can,

delaying expenditures as far as safety and efficiency will permit, to reach a time of lower prices.

The common stock of the Grand Trunk Railway, amounting, as already stated, to £23,955,437, has never in the history of the road paid a dividend. The first two preference stocks have had full dividends for the calendar years 1910, 1911, 1912, 1913, and 1916. A part dividend was paid on the third preference stock for the same years, except that of 1916. In addition to the interest which the Grand Trunk is legally liable to pay upon debentures, bonds and other kinds of indebtedness of itself and its allied corporations, it has been in the habit of paying the obligations of other companies which it is not legally liable to pay, but which it must pay in order to maintain the unit machine of its system, and which if it is to be preserved in its present earning capacity must be regarded as part of its obligations. The part that this plays in the present issue, I shall consider later on.

THE GRAND TRUNK PACIFIC

The great mistake in the policy of the President and Directors of the Grand Trunk property, which seriously injured the value of the interest of the shareholders of this property, the association of this Grand Trunk System with an enterprise for the construction and operation of the Grand Trunk Pacific Railway Company. This construction was part of a plan of Sir Wilfrid Laurier's Government for a line from the Maritime Provinces and Quebec through the northern part of Ontario to Winnipeg, in Manitoba, called the Transcontinental line, and from Winnipeg to Prince Rupert, called the Grand Trunk Pacific. Mr. Hays, as the President of the road, and Sir Rivers Wilson, as the Chairman of the Board of Directors, entered into an arrangement with the Government for the consummation of this plan. The desire of Mr. Hays and the Grand Trunk Directors was to secure merely a western connection for the Grand Trunk Railway of Canada with the Pacific coast. The Government was not content with this and insisted that there must be linked with this a line east from Quebec directly to Winnipeg. Under the contract and charter, the Government finally agreed to construct the Transcontinental line from Winnipeg to Quebec, while the Grand Trunk Pacific, a newly organized company, all of whose stock was to be owned by the Grand Trunk Railway Company of Canada, was to complete the line to Prince Rupert, a point 450 miles north of Vancouver, in British Columbia, and 450 miles nearer to Yokohama than Vancouver. The agreement provided that after the Government should construct the Transcontinental line to Winnipeg, the Grand Trunk Pacific would operate it and pay a rental yielding to the Government a proper percentage on the amount expended in its construction. The cost of both roads was so much greater than was anticipated that in 1916, when both roads were completed, the Grand Trunk Pacific officials refused to undertake to operate the Transcontinental, and in this refusal the Government acquiesced, and has operated the Transcontinental at heavy losses ever since. The Grand Trunk System did, however, secure connection with the Transcontinental line north of the lakes and thereby entered Winnipeg from the western terminus of the Grand Trunk Railway in Northern Ontario. This made a through Grand Trunk line from Montreal to Winnipeg and by the Grand Trunk Pacific to the Pacific coast. The contract required that the Grand Trunk Pacific should be constructed with the same standard of excellence as that maintained in the Grand Trunk main track between Montreal and Toronto. The result was that the cost of the Grand Trunk Pacific was excessive, as indeed was that of the Transcontinental. The Grand Trunk Pacific line runs through the Yellow Head Pass, along the headwaters of the Fraser river. This is the lowest pass to the Pacific coast either in Canada or the United States, the altitude of the track being not more than 4,000 feet. Except for twenty miles of what is called a pusher grade, where the grade is about one per cent, the grade of the rest of the line does not exceed a half of one

per cent. The bridges are of stone and steel. Material for them had to be transported by river and other expensive methods, so that the cost was greatly increased. The well-established and economical method of building such a road is to build pile and wooden bridges, temporary structures, and use them until they cease to be safe, and then to substitute a more permanent material, which can be transported over the lines of the railway at least cost. To secure the low grades of which I have spoken, the immense trestles over ravines in the Prairie Provinces and elsewhere along the line have been constructed with a view to their being filled up with dirt and thus made permanent. It would have been much more economical to begin with less favourable grades and gradually better them as growth of traffic justified it. While the Grand Trunk Pacific was being constructed in the Prairie Provinces of Manitoba, Saskatchewan and Alberta, a number of lines were being gathered together in what was called the Canadian Northern System, under the promotion of railroad contractors McKenzie and Mann. It would have been vastly more economical if the Grand Trunk Pacific and the Canadian Northern could have united in some way under the same management, and not be compelled to divide a country which could not furnish more than enough business to engage the capacity of one line. The managers of the two companies were not able to agree upon terms, and the result has been that the Canadian Northern extended its line to the coast at Vancouver, and parallels through the Prairie Provinces and the Yellow Head Pass for hundreds of miles the Grand Trunk Pacific. Mr. Hay's evident object in carrying his line to Prince Rupert, where there is a good harbour, was to make the system one for Oriental business by steamship lines organized to run from Prince Rupert to Yokahama, but in view of financial straits no such lines have been organized. Of the three more or less parallel lines in the Prairie Provinces, the Canadian Pacific, the Canadian Northern and the Grand Trunk Pacific, the gathering of business depends a good deal upon the character and extent of the branch lines. In this respect, the Grand Trunk Pacific is at a disadvantage. Its branch lines have heavier grades and are less in number and extent than those of the other lines and not so well placed.

The Grand Trunk Pacific has been operated since it opened for business on the first day of January, 1916, at a very heavy loss. It has not paid its operating expenses. The Government aided its construction by guaranteeing the interest due on its debentures issued for its building to the extent of \$68,000,000. This issue was followed by an issue of 5 per cent and 4 per cent debentures which the Grand Trunk Railway Company of Canada guaranteed. The Railway's guaranty is absolute to the extent of \$2,594,080 annually. Another guaranty is conditional on there being earnings enough to pay dividends on the guaranteed stock, but not on the Preferred and Common stock. This involves an obligation of \$1,395,170 annually. Subsequent Government aid to the Grand Trunk Pacific was given without a guaranty of the Grand Trunk Railway of Canada. The Grand Trunk Railway also advanced large sums to the Grand Trunk Pacific and its subsidiary companies from time to time. The Grand Trunk Pacific Branch Lines Company, a subsidiary company, is thus indebted to the Grand Trunk in the sum of about \$11,000,000. The Grand Trunk Pacific Development Company, another subsidiary, is indebted to the mother company in about the same sum, and so is the Grand Trunk Pacific itself in about \$267,000.

The drain upon the Grand Trunk Railway Company of Canada began before 1910, with the construction of the road, but it became heavier as the expenses of construction grew until it reached the proportions mentioned. During the years 1912, 1913, 1914 and 1915, before the Grand Trunk Pacific opened for business, and while it was still receiving the proceeds of the bonds issued for its construction, it was able to pay interest to the Grand Trunk Railway of Canada upon advances made, and indeed to repay out of the proceeds of those loans, much of the money advanced directly to the Grand Trunk Pacific by the Grand Trunk Railway of Canada. Nevertheless the net result has been the draining of the resources of the mother company

to the extent of \$22,000,000, half of which is certainly entirely lost, and can never be recovered, and the other half, that due from the Grand Trunk Development Company, may be paid ultimately, but it must be by way of salvage realized from the sales of a receiver who now holds it. The balance sheet presented on behalf of the Company of the operations of the Grand Trunk Pacific Railway System shows a deficit, after operating from the first of January, 1916, to the first of January, 1920, of \$30,845,828. Early in the year 1919, the President of the Grand Trunk Railway Company of Canada and of the Grand Trunk Pacific Railway Company notified the Government that the Grand Trunk Pacific could no longer continue to operate. The result was the taking over of the Grand Trunk Pacific as a war measure by the Government Receiver. The deficit up to the time of the receivership was \$21,415,948. After the receivership, and down to the first of January, 1920, it was increased by \$9,429,879. The net loss from rail operations, leaving out taxes, and including only railway operating revenues and railway operating expenses, from the inception of operations to December 31, 1919, three full years, was \$10,269,172. Between the first of January, 1916, and the first of January, 1920, the business of the Company, instead of increasing, decreased. It may be that the line of railway will ultimately become a valuable one. It is quite probable that the Prairie Provinces, which are so rich in the production of wheat and other cereals, and British Columbia near the line of the Grand Trunk Pacific, with its coal resources, and a steamship line to the Orient when established, may ultimately furnish large revenues to this trunk line. It is certain, however, that it will need much additional capital and a good many years' development to create a business that will make it profitable, and that if the railroad is to be maintained, it will need a very heavy maintenance fund to keep it in proper condition.

The Grand Trunk Company owning all the stock of the Pacific road abandoned it to the Government. The Government alone could take it over. They were the guarantor or owner of \$68,000,000 of its first obligations.

We cannot in this proceeding, it seems to me, attribute to the shares which the Grand Trunk Company holds in the Grand Trunk Pacific Company any value at all. The absolute guaranty, \$2,594,080, is reduced by \$301,320, which is the amount of annual interest due on the bonds of what is called the Lake Superior Line. This has been leased to the Government at a rental of \$600,000, and the rental makes complete provision for the payment of the guaranteed interest. This leaves the absolute guaranty at \$2,292,760, and the conditional guaranty at \$1,395,170, not obligatory unless net earnings of the Grand Trunk Railway, the guarantor, permit its payment after the meeting of all running expenses, interest on funded obligations and the dividend on its guaranteed stock.

Mr. Atwater argued strongly for the shareholders that something might now be realized out of a sale of the Grand Trunk Pacific to reduce the liability of the Grand Trunk Railway Company of Canada on its guaranty. I have considered this matter with care, but I can not for the life of me see any hope that by a sale of the Grand Trunk Pacific's property, a sum could be realized that would more than satisfy the first lien of the receiver's debts, which have now become \$9,000,000, and the prior debentures amounting to \$38,000,000 guaranteed by the Government.

In addition to the \$30,000,000 deficit in three years already referred to, Mr. Sullivan, a witness for the Government, and an able practical engineer, one who had served upon the Canadian Pacific and other roads, and is very familiar with the engineering problems and expense of that region, including the Prairie Provinces and the Pacific Coast, gives an estimate of twenty-four millions of money needed in the near future to keep the Grand Trunk Pacific in proper condition. A stage is rapidly approaching when the wooden structures used to maintain the grade in the form of trestles must be, by fills which are very expensive, or by steel structures. Then for two hundred miles,

in descending to the Pacific Coast, there are constant slides which promise to entail a very heavy expense in repairing them. Mr. Berry, who testified for the Grand Trunk in this matter, emphasized the difficulties and expense growing out of these slides and substantially agrees with Mr. Sullivan in his evidence as to needed fills and the short lives of these great trestles and the unwise policy in the road's too perfect construction by which its cost was greatly and unnecessarily increased.

The association of the Grank Trunk Railway Company with the Grank Trunk Pacific and the Transcontinental, is the tragic part of the story of the Grand Trunk Railway of Canada, whose history, in spite of certain indefensible acts of its London management, to which I shall refer later, is one which should arouse the gratitude of the people of Canada for the benefit which has come to them in the development of their country through the agency of this pioneer system of railways. Canada is so situated that the construction of railways with Government aid has been a political and economic necessity. It is a country four thousand miles from sea to sea, and so far as its settled portion is concerned, not more than 400 or 500 miles from north to south. Its far northwest will doubtless acquire inhabitants in the future, for it shows a surprising possibility in productiveness due to the climatic influence of the Pacific. For the present, however, the territory in which railways can find or develop business is a more or less narrow strip of settled and civilized country from east to west, with a barren interval from North Bay to Winnipeg, which is not a source of useful products, but must be traversed in order to reach from the east to the Prairie country and to the Pacific.

It was made a part of the condition of the union, embodied in the British North America Act, that Quebec and Ontario should be united by Railway with the Maritime Provinces and the Government was obliged therefore, as a political necessity, to build, construct, own and operate at a loss the then called Intercolonial Railway.

A condition of the coming into the Dominion of British Columbia was an agreement that a railroad should be constructed uniting the Pacific Coast with the eastern provinces of Canada. This had to be done and was done by private enterprise, reinforced by very large contributions from the Government. The history of the Canadian Pacific and its present wonderful prosperity finds something of its explanation in the fact that the Government contributed very largely to its construction in actual outlay and the actual building of important parts of the road, and also in its land grants. These have enabled the company to maintain a very low capitalization in its bonds and stocks, and therefore to earn substantially a constant dividend on its capital stock, perhaps as certain and as ample as that of any railroad on the continent.

The Canadian Northern, too, has had very extensive government aid, even greater in proportion than that of the Canadian Pacific. The Grand Trunk Railway Company of Canada, which was much earlier in the field, and offered the opportunity to Ontario and the western part of Quebec to develop prosperously, has had comparatively little assistance.

All these circumstances should challenge, on the part of those who are called upon to do justice to non-resident shareholders, the closest attention to the pleas made in their behalf and to the exercise of a spirit of equity in dealing with their interests, which are now to be ended in this enterprise and are to be compensated for by our adjudication and award.

It was for this reason, among others, that it seemed to me a proper course to allow the company and the shareholders to offer in evidence proof of the reproduction value of the whole Grand Trunk Railway System and of what is called the physical value of the property as distinguished from the reproduction value. This would not be for the purpose of compelling the Government to pay the reproduction or actual value of the physical property, but only to enable us to use the value as a circumstance in judging its future and potential net earning capacity. Such evidence is held in

the United States to be competent and relevant in adjudging what a railway company should earn and therefore to fix its rates. With conditions so much the same in both countries and in respect to a railway like the Grand Trunk, seventy per cent of whose rate receipts are directly affected by rates in the United States, it would seem proper to adopt the same rule of evidence.

In a similar proceeding by the Government taking over the Canadian Northern, through a Board of Arbitration, at the head of which was the Chief Justice of Ontario, received evidence of the reproduction value and acted on it in their award. The Government filed there a formal objection but did not press it and the evidence went in. Evidence of this kind here produced might have materially affected the opinion which the Board would form of the earning capacity of the road and its future possibilities, especially in view of the fact that the tendency of railway legislation in the United States, as shown by the last United States Transportation Act, is toward making the reproduction value of railroad property used economically for transportation a proper basis for fixing rates. The ruling of the majority of this Board, however, has been against receiving such evidence. Bowing to that decision, it becomes my duty, as a member of the Board, to fix the value of this stock without the aid of such evidence.

One of the great issues made in the case is as to the physical condition of the road and the system for operation. The Government has been at great pains to point out the defects of the road and the failure of the company to expend the needed funds for current maintenance of bridges, rails, ties, ballast, the motive power, including locomotives, freight and passenger cars. On the other hand the counsel for the shareholders insist that the history of the road and its achievements during the war and under the stress of greatly increased traffic, is an indication that it is safe and one hundred per cent efficient—that one must judge of a road by the work it does and if the freight is carried and the passengers are carried without accident or loss for years, and the duty of the common carrier is thus discharged, and the equipment of the road is kept up to such a point that the work to be done is done, it can not be said that the road is suffering from any great deferred maintenance.

The chief witness for the company was Mr. John B. Berry, a railway engineer who has had a long experience in the engineering department of the Chicago and Northwestern Railway Company, a most important and extended system, and thereafter Chief Engineer under Mr. Harriman in the great reconstruction of the Union Pacific Railway Company, and then for six or seven years the Chief Engineer of the Chicago, Rock Island and Pacific Company. Mr. Berry is a man of the highest standing in the railway engineering profession. He may be looked upon perhaps as the "dean" of that particular branch of his profession. He is a man evidently of solid character and of strong opinions which he does not change at the suggestion of counsel, either of those who call him or those who cross-examine him. He has visited the principal lines of the Grand Trunk Railway of Canada many times and the properties of all its subordinate companies, as well as those of the Grand Trunk Pacific. He examined the records of the properties of the company before he made his inspection, made up his mind as to the bridges and places on the road at which he would stop, and give close inspection. He noted the condition of the rails, of the ballast and of the ties from an inspection car placed in front of a locomotive which ran some 15 miles an hour, and which stopped wherever he indicated his wish to do so. He made notes of his examination and reported what he saw as either "good," "fair" or "poor." "Good" meant a high standard, "fair" meant something that would last for four or five years but would then need to be replaced, and "poor" something that ought to be replaced in the near future. He did not make an inspection with a view of reporting on the cost of making the repairs that might be needed, but he made a report as an experienced engineer would make it, in giving to one considering the question of purchasing the property, a satisfactory knowledge

of the condition and the value of the road. In fact he did prepare a report of its reproduction value, less depreciation, though he was not allowed to put it in evidence. He made this report with full appreciation of the judgment that those who engage in the actual economical operation and maintenance of the road with limited resources must exercise, in determining the amount of current repairs and maintenance that should be made to keep in good operating condition. Mr. Berry's evidence is that the railroad does not show deferred maintenance but on the whole is in excellent condition.

The Department of Railways and Canals of the Canadian Government, on the other hand, sent out a force of men to make minute examination of every part of the road and to report on every deficiency which they could see, with a view of estimating what it would take to repair and equip the road according to a standard not affected by a limitation of means, but with the backing of a government treasury, and with a knowledge that the report was to be used in depreciation of the value of the road to be bought. I have no criticism to make upon the witnesses for the Government except to say that there was on the part of Colonel Montserrat, who reported upon the bridges, and the others who reported on the maintenance of way, an enthusiasm of condemnation that rather injured the weight of what they had to say, with me. Colonel Montserrat's evidence was so rebutted by the evidence of those who were in constant charge of the work that he criticized as to give me the impression that he was calculating the cost of producing a perfect road without regard to economical considerations. His severe criticism of bridges which in the growth of business had grown too light for the traffic, and had been strengthened by the use of wooden or pile bents, seemed to me to be unjustified, and I must agree with Mr. Berry's criticism and with that of counsel for the shareholders that upon lines where the traffic is light, where the profit from the operation is small, if any, but which must be maintained, the use of pile bents to continue the life of bridges is much wiser than the expenditure of a large amount for new steel structures when the bridges thus reinforced will last for several years and be entirely safe, and this however much they may offend the eye of an engineer who insists on new and good-looking bridges everywhere. The tone of Colonel Montserrat's statements as to the bridges was likely to give the impression that the condition in many instances are dangerous, and yet the fact is that the road has been operated under the same conditions for a number of years with complete safety, with these bridges always under observation, and with an accurate knowledge by the men in charge of the status of each bridge and any change therein for years.

It may seem an anomaly to criticise the reports of witnesses in respect to the condition of the railroad as too minute and meticulous, and yet the criticism is not without justice. It reflects the purpose to dwell on small deficiencies, to insist on perfect reparation of them when a reasonable economic policy would lead to a less expensive method by which complete safety and effectiveness can be secured without a large outlay for some years, until a time of cheaper construction and easier money. Thus a recommendation that great grain elevators made of wood and reasonably effective for their purpose for years to come should be torn down and new elevators put up of reinforced concrete, made by a witness for the Government, seems to me quite unreasonable, and this even though the insurance of grain when warehoused in wooden elevators is greater than that in a concrete warehouse. The record shows that there are many, many wooden elevators in active and profitable use, and the mere fact that when new elevators are built now they are built of concrete does not justify a policy of pulling down perfectly good elevators made of wood. The reason for constructing concrete elevators now is not due solely to a desire to reduce danger of fire but also because of the very high cost of timber.

I do not wish to impeach the veracity or professional skill of the Government experts on this issue of the condition of the road and the needed capital and main-

tenance expenditures. If the Government wishes to adopt the policy of putting the railroad in pluperfect condition and reduce further maintenance to a minimum for a series of years, and to make these expenditures now when the cost of everything is much higher than it is likely to be, that is a matter of policy with which we here have nothing to do. But when evidence of such cost is used to show how impossible it would be for the Grand Trunk to avoid heavy and overwhelming deficits in the near future and thus destroy all potential value of the stock of the Preferred and Common stock shareholders, I feel that I should doubt its weight for that purpose. In order to put the Grand Trunk System into proper condition, the sum of the estimates of these Government experts is that it would cost the Company in five years seventy-four millions of dollars, of which forty-four millions would be non-remunerative capital, \$8,700,000 would be remunerative capital, and \$21,881,010 deferred and extraordinary maintenance. When the budget was prepared by the officers of the company to be presented to Parliament for a vote of the budget of the year of money to be paid out by the Company under the operation of the Company for fifteen months, ending March 31, 1922, the amount of it was \$44,000,000. The Department of Railways directed that the budget be returned and that it be increased to \$89,000,000 which was accordingly done by order. One of the chief differences was an additional sum of \$16,000,00 for capital and other expenditures for maintenance. As recommended by the Government experts, the officers of the Company charged with the safe and efficient operation of the railway system did not deem such a sum necessary at this time.

The counsel for the Government press upon the Board, as corroborating their witnesses as to needed capital and maintenance, a report made by Howard G. Kelley early in 1917. Mr. Kelley, now the President of the Grand Trunk, was then the Chief Engineer of the system. At that time the President, Mr. Chamberlin, and London management of the company were seeking to induce the Canadian Government to take off their backs the burden of their Grand Trunk Pacific investment and to restore to them the moneys which the Grand Trunk had put into the Grand Trunk Pacific enterprise. They were anxious to make a showing of poverty on the part of the Grand Trunk Railway of Canada, and of the impossibility of its continuing if loaded down with the Grand Trunk Pacific. They therefore understated their actual revenues in their published reports by some millions. This is the contention of counsel for the Government, which is not disputed. Their President, Mr. Chamberlin, testified to the Railway Commission, appointed for the purpose of investigating the Grand Trunk and the other railways of Canada, and the then condition of the Grand Trunk in the matter of maintenance, and greatly emphasized it. At that time, as a matter of fact, and by the admission of Mr. Kelley on the stand in the present case, the maintenance had run down because of war conditions, and the difficulty of securing labour and material. Mr. Kelley, as Chief Engineer, and under the instructions of his superior officers, thereupon made a report upon the needed expenditure capital and current for the purpose of putting the Grand Trunk into a proper condition. It is manifest, from the report itself, as well as from the circumstances, that by direction of his chiefs he prepared this report in accordance with the standard of the same kind of perfection as that which Colonel Montserrat and his fellow witnesses for the Government have prepared their report in the present case. He laid down a measure for the renewal of rails and of other equipment which considerably exceeds in its requirements even those of the Government witnesses. He was not then President of the road—he was merely the Chief Engineer acting under the directions of his superior officers and using that discretionary judgment that may have a very wide range in stating a *de luxe* estimate of needed expenditures and needed maintenance. Since that time in the years 1918, 1919 and 1920 a very large amount of money—forty-seven millions—has been spent in putting the Grand Trunk Railway into

better condition after the war. Mr. Kelley has been on the stand and testified at great length as to the present satisfactory condition of the road for the efficient discharge of the duties of the railway company. He has told of the heavy traffic that is carried on during the war, and he speaks with confidence of its condition with which he is most familiar, and of its capacity to do a much larger business than it now does, without any extensive additions in the matter of capital and maintenance. Counsel for the Government were at liberty to cross-examine Mr. Kelley by reference to his report as Chief Engineer and thus call from him an explanation of the difference between his present statement as to the condition of the road and his report of 1917. Instead of this, they put in his report without any further cross-examination of him. It is suggested that counsel for the company have said that they were going to reproduce him on the stand with reference to deferred maintenance. Counsel for the company say that they did not carry out their purpose because of the ruling of the Board as to incompetency of the evidence as to value. It is only sufficient to say that if the Government counsel had desired, Mr. Kelley was available for cross-examination after the introduction of his report, but he was not recalled for that purpose. We are left, therefore, with his statement in chief, his explanation of the present condition of the road when he speaks as the responsible President of it, and with this earlier report of his in 1917, made under instructions and under the circumstances which I have already described. In order to make up for the condition in which the war had left this railroad, as it had all other roads, the management of the company had spent large sums for maintenance amounting in 1918 to nearly 12 millions, in 1919 to 17 millions and in 1920 to 18 millions, and it is insisted by counsel for the company, and testified by Mr. Kelley, Mr. Berry, and the company's officials in immediate charge, that this sum put the road in as good condition as any road in the country, and that such capital expenditures as the Government urges as indispensably necessary are not so.

I should observe at this time that while the date, May 21, 1920, is the day when the stock is deemed under the contract to have passed to the Government, although the shareholders through representation in the Committee of Management still retained some control until June, 1921, evidence as to money spent in the improvement of the road after that date, out of the income from the road, is not rendered irrelevant. More than this, there is evidence that ties and rails had been bought by the company before the date of transfer, which were subsequently put in place. One can not strike a balance as of a day like the 21st of May. We must consider a railroad by years. Its accounts require it. It is a going concern and must be so considered and treated in its condition and valuation. It is fair, therefore, for purpose of determining the kind of railroad in which the Government is acquiring stock control by the purchase to bring the condition of the road down to the end of 1920.

It will be observed that the \$74,000,000 of the total proposed by the Government for the years 1920 to 1926, includes \$43,000,000 for the grade separations, already referred to. This is to be done in five years when even the witness upon whom reliance is had for this estimate expressed the opinion that it would be twenty years before the railway would be obliged to meet the full weight of such a burden. Such an item does not lend force to the exhibit as a whole. It does tend to make it especially persuasive in trying to estimate what the Grand Trunk Railway, if left in possession, would have to spend wisely and economically to keep its railway system up to do its public work safely and efficiently. These large sums are then introduced into the future estimated accounts of the company and pile up the fixed charges of the company so as to increase them some seven millions by 1925, which would preclude all possibility of dividends on the preferred stock. In other words, it is proposed to put a seventy-five million mortgage on the Grand Trunk property now as essential, with the result that the shareholders' interest disappears under the increased

annual charges. I must feel that the evidence of the witnesses for the company is more weighty upon the point here in issue, namely what would a reasonable, economical owner of the railway have been able to work out for his shareholders in the next few years after having operated the railroad sufficiently and economically and safely, and having paid the fixed charges. My point is that the witnesses for the Government have directed their evidence to the cost of a policy in dealing with the railroad, which is not one which a private owner with the limitations upon his expenditures, not mandatory upon a great Government, would pursue.

Mr. Butler and Mr. Tilley have urged, with great force and ability, the view that the road can not be in good condition now because the Company did not pursue a proper course in setting aside a sum each year for maintenance to meet the depreciation that time necessarily brings. Mr. Butler referred to a direction of the Interstate Commerce Commission as to a head for depreciation in its classification of accounts to be kept and reported, a rule which the Canadian Railway Commission has not yet adopted, and which indeed is not fully in force and hardly more than recommended by the Interstate Commerce Commission itself. Cases have been referred to in which the Supreme Court of the United States and Sir George Jessel, the Master of Rolls, have emphasized the duty of directors of a company to make provision for repairs and maintenance and necessary renewals and not to declare dividends out of the gross earnings when nothing has been set aside for these purposes. There is no doubt about this principle, but we are not here for the purpose of determining whether the dividends which were declared should not have been declared, any more than we are for the purpose of punishing the directors for juggling with their accounts. We are here for the purpose of determining what the real interest, if any, in this railroad property the shareholders have, and what value, if any, it has. We are interested in the actual condition of the property, and while it is true that rules as to what ought to be done with reference to maintenance, in the view of an expert Commission like the Interstate Commerce Commission, and the failure to comply with their judgment in that respect may have a tendency to show that the road in question is not in proper condition, direct evidence as to its condition is more weighty, and the old argument that "proof of the pudding is in the eating," has application. However faulty the managers of the road may have been in not establishing a depreciation reserve and in not at different times spending it as such, the fact remains that through the critical period of 1916, 1917, 1918, 1919 and 1920, this Grand Trunk System did an enormous work and never failed to meet the very exigent requirements of the Government in its transportation of the things which were so much needed to win the war. Moreover, it is true that however improper the motive for the establishment of an audit office account, the result of it was to furnish in 1919 and 1920, a large reserve fund to expend on the property by way of maintenance and renewals. No evidence has been offered to rebut the statement of Mr. Williams that in the earlier years a large amount of what might properly have been charged to capital investment was taken from the earnings of the road to keep up the motive power, the locomotives and the cars, and, as already pointed out, there is substantially no evidence to show that the cars and locomotives now owned by the Company are not ample for all the business that it is already doing or is likely to do.

The operating efficiency of the railroad can not be denied. The Company is to-day and has been for years last past, operating fast trains, numerous trains and heavy trains, the trains are making schedule time and there are substantially no accidents. Although these operations and the records of the Company have been completely under the scrutinizing and critical eye of government experts, no evidence has been adduced to rebut this. No attack has been made upon the tractive power of the Company. Several competent witnesses, after close inspection, have testified to

proves it. The same thing is true of the freight and passenger and other cars. The shops and round houses, except in a few spots of comparative unimportance, which can be remedied by very moderate expenditure, are in first class condition. As to the ties, the question is a matter of wise judgment. Mr. Berry's long experience and close examination of the records of the operation of the road enabled him to fix a proper standard of annual tie renewal at 2,000,000 a year, or 264 ties to a mile and the railway records show that taking one year with another, the renewals, including 1919 and 1920, have averaged 265 a mile a year. In respect to rails the showing is not so good because it was impossible to secure suitable rails during the war, and still more difficult to get the labor properly to replace them. The standard set by the Grand Trunk for its main double track from Montreal to Chicago and the New York territory has been one hundred pound rail, and much more than three fourths of it is of that weight. It could only secure under government limitation during the war period, 85 pound rail. During 1919 and 1920, a large amount of new 100 pound rail was purchased and put in the year following, considerably more than average yearly renewal. Mr. Robb says that more rail was put in the road in those years than in any year since 1907 and 1910. From Mr. Phippen's reference to the exhibits it appears that with the exception of grade separations, docks and wharves and elevators, the amount recommended for 1920 for maintenance, including bridges, rails, ties, ballast, etc., by the Government experts was \$15,901,000, while the Company actually spent in that year \$15,226,000 on the same things. It is true that Mr. Butler remarked that his witness advised him that the two did not cover all of the same things and that there was 7 millions in which they did not overlap, but this has not been explained.

I have already spoken of grade separations and elevators.

In reference to docks and wharves, a word is proper. These docks and wharves upon which Government witnesses insist much should be spent, are most of them at the termini of branch lines of the Grand Trunk where the business is very light indeed and unprofitable and in respect to which a policy of the severest economy consistent with safety is the one on the basis of which we must place our judgment and estimates, and not one of expensive renewals or complete rebuilding.

On the whole evidence, when the fact as to what the great system is doing and has done for a long series of years, is considered, I can not bring myself to credit an unfavourable and condemnatory description of the condition of this old and settled railroad property, that would require for its continued practical operation for useful public purposes, an investment of what is equivalent to form seventy-five millions of new capital. We must, I think, resort to other means of judging the requirements of the situation.

I do not deny that the government plan of advancing large amounts of capital at the present time to improve the road and reduce the expense of maintenance in the future may be the wise course for the Government to pursue in carrying out its purpose in establishing the Grand Trunk System under government ownership. It is not, however, the most economical at such a time as this. Such a policy by Mr. Harriman in the reconstruction of the Union Pacific has proven itself to be wise, but a policy like this can only be carried out by those who are willing to wait decades for results in the form of net earnings and who have the financial ability to meet the immediate expense and delay returns for a considerable period. That is not a policy which can be used as a guide in a case like this to determine what the value of shares of stock are in earning dividends within a reasonable short time. It sacrifices much of railroad property capable of further profitable use, and if the stockholders had retained their interest, it would ignore their right to the most economical performance of the railway's public duties consistent with public safety and efficiency.

In a case like this, it is perfectly natural that witnesses should have a leaning toward the side which calls them, with a knowledge of the purpose for which they are called, and the Board must weigh the evidence in the light of the circumstances and attempt to reach in its judgment the probable fact. My own judgment is that the actual facts lie between the views of the opposing witnesses and that while there is a necessity for better maintenance in the Grand Trunk System which may delay somewhat a return to a normal net operating percentage, after the strain of the war, the reports of the governmental engineers are quite excessive. They pile Pelion on Ossa.

We come now to the principal and ultimate question of the case upon which what I have been discussing has a bearing. That question is what we may reasonably anticipate as the net earnings of the three Preferred stocks and the Common stock within such a time that an intending purchaser would be practically affected in the price he would pay for them.

In presenting to the court the various elements of value of the Grand Trunk road, Mr. Phippen first dwelt upon certain properties which he denominated as "frozen assets." He considered that they amounted in ultimate realizable value to \$25,000,000 or more. The first of these was the property of the Southern New England Railroad Company, a railroad projected and partly built between Palmer, Massachusetts, and Providence, Rhode Island. This railroad was begun by the Central Vermont and the expenditure was made by it of \$7,000,000 loaned for the purpose in 1911 by the Grand Trunk Company without interest. The right of way has been purchased and a good deal of the grading has been done, but it would take some \$7,000,000 more to finish it. It is a railroad which if built would give access to Providence, Rhode Island, to the Grand Trunk System and would bring that system into a territory in Massachusetts, Connecticut and Rhode Island, which is a hive of industry, and would doubtless be a source of much increased business for west bound traffic over the Grand Trunk lines. Mr. Kelley does not recommend the investment of any further money in the completion of the railway until times change and prices fall, but his judgment is that in the future it will be wise to complete the road, and that the road will become a profitable feeder for the system. It seems to me that the road may be made profitable some years hence.

The Jacques-Cartier Railway running around the mountain of Montreal to connect the main line of the Grand Trunk with the territory east of Montreal to the river is another unfinished investment that brings in now nothing but obligations in the form of taxes. How valuable this may prove to be in the future is a matter of speculation and upon which we have no means of judging except by the cost of it, which was \$1,600,00.

The next item in this list of "frozen assets" is the indebtedness of the Grand Trunk Pacific Development Company to the Grand Trunk Railway of Canada. This indebtedness grew out of advances made by the latter company to this Development Company to enable it to carry on the business of assisting the Grand Trunk Pacific Company in its building and operation. It owns steamship companies, dock companies, hotel companies and a good deal of land for sale. It has not paid a dividend because from much of its property it is not expected to secure a regular income but merely to develop it and then sell it and divide the proceeds. It owes \$11,000,000 to the Grand Trunk Railway of Canada, and \$2,000,000 to the Grand Trunk Pacific Company. It was taken possession of by the receiver whom the Government put in charge of the Grand Trunk Pacific Company. The Grand Trunk counsel insist that this is a breach of the rights of the Development Company because it was not insolvent and the Grand Trunk was its largest creditor. We have not had specific evidence adduced before us as to the value of the properties which it holds. There is \$3,000,000 outstanding in payments due upon lands sold, and there are two large fine hotels, the Fort Garry Hotel at Winnipeg, and the McDonald Hotel at Edmonton,

which cost millions, and are valuable and likely to be profitable. The assets of the Development Company, as shown by its books, amount to \$12,536,324, as follows:—

Hotel property.. . . .	\$5,719,108
Wharves and docks.. . . .	3,859,624
Steamships.. . . .	1,273,135
Company holdings.. . . .	7,719
Gravel lands.. . . .	37,236
Terminal lands.. . . .	292,745
Rights of way.. . . .	3,932
Mortgages on employees' houses.. . . .	11,135
Cost of farm lands.. . . .	1,331,690
	<hr/>
	\$12,536,324

They indicate a very considerable salvage in the claim for \$11,000,000 which the Grand Trunk has against the Development Company when the other debts are only two millions.

The fire insurance fund accumulated by the Grand Trunk of more than a million dollars, in order to do its own insurance, would seem to be worth its face in that it saves the Grand Trunk from the annual payment of a very considerable amount for current insurance and this reduces its operating expenses. Another fund of a similar character is the compensation fund of \$350,000 which adds value to the Grand Trunk Railway Company certainly to the amount of its face, by reason of offering indemnity against claims for damages for injuries that are a constant source of expense.

The next item is the investment of some \$2,000,000 in the Montreal and Southern Counties Railway. The operation of this railway has resulted at times and for some years in the earning of a small surplus over and above expenses. For the last three or four years, however, there has been a deficit of about the same amount each year. The Grand Trunk has \$340,000 of the stock, with \$100,000 held by the public, and in addition the Grand Trunk has \$500,000 of the stock issued or to be issued to reduce its indebtedness. I was much impressed by the evidence that this company will in a few years become a paying investment. It serves a series of rapidly growing suburban towns south of the St. Lawrence river within easy reach of Montreal, not only for commuters but also for the carriage of milk and for express and other freight. It has not made any provision for depreciation and may need further capital to confirm its success, but I have a strong feeling that the property is one which will turn out to be profitable.

The Rail and River Coal Company owns 30,000 acres of coal land in south-eastern Ohio. The coal is of the Pittsburg vein and is excellent steaming coal. The value of the property is estimated by Mr. Walter Kelley, the Superintendent of the Mines, as worth \$12,000,000. An estimate by an expert connected with the geological department of Ohio was \$8,000,000. These views were contradicted by a witness of some experience in coal lands, but who it seems to me did not qualify himself as the other witnesses were qualified. It is quite certain that the mining plant is well managed and is well equipped with the best modern machinery, that a very considerable amount of money has been expended in perfecting it, and that an adequate depreciation fund is provided. It is also clear that a good deal of the unused land has a definite market value per acre. Of course the value of the property will be much affected by the general situation of the coal market, questions of strikes and otherwise, but in this proceeding when the value must be fixed, we must assume a return to normal conditions and a demand for coal which the resumption of business will certainly create. I am inclined to think that the estimate of Professor Ray as to the value of the mines and property of this company was not in excess of its real value now that the mines can be economically operated with the best machinery and the surplus lands can be disposed of with reasonable care and discretion. To put therefore the unused land in among the frozen assets at a figure of \$3,000,000 would

be fair, leaving the full amount of land for years to come for mining purposes still in the possession of the Rail and River Coal Company.

A question has arisen over the title to the stock of the Rail and River Coal Company and a good deal of evidence is submitted. This has given me no difficulty. The argument of Mr. Lafleur upon this head is entirely satisfactory and convincing. The history shortly stated is this: Mr. Hayes became convinced that it would be wise to acquire this coal property to be used in connection with the operation of the Grand Trunk Railway in furnishing at a low cost good steaming coal for that part of the railroad that could be reached by a reasonably short haul. He was anxious to acquire it, but he could not induce the Board of Directors to take over the property to the Grand Trunk road chiefly for the reason they were advised that the charter of the Grand Trunk would not permit it to operate a coal mine. Moreover, there was fear that the commodity clause of the Interstate Commerce Act would forbid a railroad from owning a mine for such purpose. As a matter of fact, neither of the objections proved sound. However, the property was taken over in the name of the Development Company and contracts were formally made with the Grand Trunk Railway for the delivery of coal. The money for the purchase price was paid by the Grand Trunk Railway of Canada, and notes were given to the Grand Trunk Company for this. While the Directors were thus loath to assume the ownership the property was carried in what was really a state of suspense as to the title for several years. In spite of a good many formalities inconsistent with the real fact, it seems to me that the truth was that Mr. Hayes and those in charge always considered that this property belonged to the Grand Trunk Railway Company, which had paid for it, and were only waiting until the unfounded fears of *ultra vires* on the part of the directors of the Grand Trunk road were removed before vesting the title to the stock formally in the Grand Trunk Company. Some two years before the initiation of the receivership of the Grand Trunk Pacific Railway Company, which embraced that of the Development Company, the Grand Trunk directors gave authority to the officers of the Company to take over to the Company the stock of the Coal Company. This authority was not formally exercised until just before the receivership. It is said that this formal transfer, effected just before the receivership, was a fraud upon the creditors of the Development Company. As the Grand Trunk is the only creditor of the Development Company, except the Grand Trunk Pacific Company, the debt to the former being eleven million and to the latter two millions, the motive for the fraud is not apparent. In fact, the transfer was in my judgment nothing but the commendable formal execution of either a resulting or an express trust. The mines are a valuable adjunct in the operation of the Grand Trunk Railway. All of the land is not needed and a part might well be sold. In the estimate of frozen assets, it would not be unfair to put this extra coal land in at three millions of dollars. The last of these assets is the amount of land purchased by the Grand Trunk in Montreal for enlargement of the approaches to the Bonaventure station in Montreal, the original cost of which Mr. Phippen doubtfully estimated at half a million, but the interest charged to the purchases indicates that it was about three millions. It will be available for use in grade separations and establishing new terminals in Montreal. Mr. Phippen's claim is that these frozen assets at a fair estimate are worth \$25,000,000. It is possible that this is too rosy a view of what their value is, but certainly I should think that \$20,000,000 could be realized from them in the course of the next ten years, and that they may be regarded as an offset to the amount of money likely to be imposed as an obligation upon the Grand Trunk System for grade separations in Toronto and Montreal, Detroit, and Chicago in that time.

Counsel for the shareholders have urged three different ways of proving that in the near future enough may be earned by the company to pay all that the contract and statute permits the Board to award to these stockholders.

The first agreement is based upon quotations taken from the London Stock Exchange and covering some four or five years, ending with 1913. In the discussion

of the competency of evidence as to reproduction and physical value, I said that in my opinion little or no weight should be given to quotations on the Stock Exchange, especially where the stock has speculative value, as this seems to have had. Where the question is between one who has bought and one who has sold, and of damages for a breach of contract of a sale of a block of stock, the stock market quotations showing what might have been realized for the block at a particular time, or what stock might have been bought for at a particular time, would be relevant and important evidence in determining the rights between the vendor and purchaser, but here is where the Board advised as to all the facts in respect to the financial condition and earnings and management of the company—facts that could not be known fully to the public or those engaged in dealing in the shares, and where the purchaser is to buy the whole issue of stock, I do not myself feel that the quotations are useful at all. These quotations were quotations in 1913 made before the company had been greatly affected by its association with the Grand Trunk Pacific, and while it was receiving interest on its advances to that company. This Board is warned in the very statute under which it is acting not to take into consideration, as a means of determining the issue here, stock quotations if they are effected by the negotiations between the Government and the company. On the other hand, to go back to the quotations before the war, when so much has happened detrimental to the Grand Trunk Company since, is to resort to evidence of the most unsubstantial character.

The next basis for the claim of counsel is based on the provisions of the new transportation act of the United States. It is said that because the Esch-Cummins Act ordered the Interstate Commerce Commission to establish such rates as would return to the railway companies in the United States not less than $5\frac{1}{2}$ per cent and not more than 6 per cent on the value of all the property of those companies devoted to the public service, and the relation of the Grand Trunk System to the American Railway System is so close in that 70 per cent of its rates are affected by the rates of the United States that we must assume that the action of the Interstate Commerce Commission under the Act will bring a net return to the owners of the Grand Trunk of 6 per cent on the value of their property. On this basis counsel for the company urged the relevancy and competency of the reproduction value and actual physical value of the Grand Trunk properties. That evidence was rejected. In the absence of such evidence, I do not think there is any basis of comparison under the Transportation Act and can not follow Mr. Phippen in his argument on this head.

The third argument of Mr. Atwater and Mr. Phippen is based upon the normal net earnings of the Grand Trunk in the past and their amount having regard to the steady increase in the total business of the railway and its operating revenues.

Before taking this up in detail, I think it proper to consider the conclusion which the Chairman of the Board has reached, that on May 21, when the transfer of title to the stock probably vested, the company was bankrupt, and therefore that the shareholders, the value of whose interests in the company we are considering, had nothing then in the company which we can value. The value we have to determine is, it is true, the value of the shares in May, 1920, but their value in May, 1920, is determined not by the limited earning capacity of the company at that time if there was a reasonable prospect that within a few years its earnings will be greatly increased. I agree the injury done to the property by the war and the absolute losses thereby suffered, those interested in it, bondholders and shareholders as well, must accept as a reduction in the value of their property, but they are not to be held to an earning capacity as of that date. They are entitled to a value then reflected by the prospect of a return to better conditions and an earning capacity within a reasonable period such that the earnings may meet not only the fixed charges but also furnish a dividend on the capital stock. We have a right to exercise our judgment as to when a normal condition of affairs will come, and on the basis of our judgment to judge the normal earnings in the future by the normal earnings in the past. More than this, if it be

true that the volume of the business done by the company, and which the company is able to do, in spite of the untoward conditions, has shown a steady increase in the amount of business done, at a regular ratio we have the right to predicate an increase in the future. Normality in respect to the Grand Trunk Railway of Canada is one that can be much more safely reasoned about and acted upon than in the case of a new railroad as the Grand Trunk Pacific. We can be quite sure that if other railroads in the country are returning to a normal basis, the Grand Trunk is likely to do the same thing. To say that the Grand Trunk on the 21st of May, 1920, at the nadir of railroad prosperity in the world, when purely operating expenses were as abnormally as large as they were, was in a state of bankruptcy, and the interests of its shareholders worth nothing, is, it seems to me, to deal most inequitably with the shareholders. Who can say what would have happened to the Grand Trunk if the Government had not taken it over? Had the Government not come to the rescue, it is quite possible that the bondholders who had already come to its rescue in 1860, might have aided it again, with the confidence that by tiding over the then exigent situation, they could count on a return to the normal.

I may add with reference to the views of the Chairman of the Board as to the bankruptcy of the Grand Trunk, that they are based largely on the Drayton-Acworth report and its contents, made now more than four years ago, in 1917. That report was admitted in evidence as reflecting on the value of stock quotations and for other limited purposes, and its use as evidence by way of admission against the company, or its shareholders, was distinctly disavowed by counsel, and as I understood it, that disavowal was approved by members of the Board. This is apparent from the record from which I quote at length.

"Mr. TILLEY: The question was raised before adjourning this morning as to the admission of the Drayton-Acworth report. I suppose my friends are ready to take a stand on that.

"Mr. LAFLEUR: Of course, this report is not strictly evidence except that a certain recommendation was made by a Government Commission. At the same time I do not know that we have any serious reason for objecting to it, provided it is understood that the statements which are there made as to the company's financial standing, or as to the deferred maintenance is not binding and we are not to be considered as admitting those statements at all because we consider that that question must be decided by the evidence which has been adduced before you.

"The CHAIRMAN: No question about that.

"Mr. LAFLEUR: And we wish to be at liberty to criticize those findings if they are urged against us, and to show that those Commissioners erred in their statement of the company's liabilities, and in the statement as to the deferred maintenance, because they made no distinction between deferred maintenance and deferred improvements.

Subject to these observations, we are not strenuously opposing the introduction of this as a sort of historical document. It is a public report.

"The CHAIRMAN: There is a portion of that report, Mr. Lafleur, that struck me as not admissible. It is the evidence that is quoted of Mr. Chamberlin and said to be corroborated by Mr. Kelley. I may be wrong about it, but I would have thought that was not admissible.

"Mr. LAFLEUR: No, because we had no opportunity of cross-examining these gentlemen, it was an ex parte examination.

"The CHAIRMAN: It could have been used while Mr. Kelley was in the box by confronting him with the evidence he gave then. The question of Mr. Chamberlin's evidence raises another point.

"Mr. LAFLEUR: We are prepared to show that Mr. Chamberlin, in his answers there, was not familiar with the situation, and that he made no distinc-

tion between deferred maintenance and deferred improvements which are chargeable, respectively, to income, revenue and capital.

"Hon. Mr. TAFT: I understood that Mr. Kelley's statement had already gone in as evidence.

"Mr. TILLEY: His statement went in yesterday.

"Hon. Mr. TAFT: As an admission by the company. That is what I supposed it did.

"The CHAIRMAN: I didn't understand that. I don't remember it, and more than that his evidence is not stated in this report.

"Hon. Mr. TAFT: Mr. Butler introduced the evidence, and there was no objection to it. At least I didn't hear any.

"Hon. Mr. ATWATER: Just at the last moment last night Mr. Butler introduced Exhibit 444 which he stated to be the letters written by Mr. Kelley to Sir Henry Drayton in connection with this examination that he was making. We did not have an opportunity to object to the production of them at the time, and Mr. Butler, when he produced them said he was just giving notice that he was going to produce the letters.

"The CHAIRMAN: It is a statement made by Mr. Kelley, corroborating Mr. Chamberlin.

"Mr. LAFLEUR: In which he furnished Sir Henry Drayton with certain statements. Now, it seems to me, if my learned friends intend to rely upon that, they ought to examine Mr. Kelley as to that, because there are explanations which must be given in order to make them conform with the evidence actually before you.

"The CHAIRMAN: That is a different question from what we are discussing. That is a letter from Mr. Kelley regarding information asked for by Sir Henry Drayton. The point we are discussing now is whether the evidence stated to be given by Mr. Kelley before the Commission is admissible.

"Mr. LAFLEUR: It is annexed as an appendix to the report and, of course, I would respectfully submit that you should not consider that at all.

"The CHAIRMAN: As I recollect it, there is no evidence which is appended to the report as having been given by Mr. Kelley. There is only the statement made by Sir Henry Drayton that Mr. Kelley was sworn and corroborated.

"Mr. LAFLEUR: I am saying that you should give no consideration either to the evidence of Mr. Chamberlin in that report or to the alleged corroboration by Mr. Kelley, because you have the evidence in this case upon this question.

"The CHAIRMAN: They ought to be confronted with the evidence.

"Mr. LAFLEUR: If that report simply goes in as a sort of historical record that the recommendation was made to the Government to deal with the railways in a certain way, we have no objection, but if it is intended to refer to that evidence, or to that admission, or to the findings, as binding upon us, or as evidence before you to assist you in coming to your award then we object.

"The CHAIRMAN: Of course, they were seeking to get \$25,000,000 at that time, and it was up to them to give certain evidence that does not exist to-day.

"Sir THOMAS WHITE: It seems to me that what Mr. Lafleur says is sound. Evidence taken in the inquiry by the Drayton-Acworth Commission would not be evidence here. If Mr. Kelley was in the box I suppose it would be quite proper for Mr. Tilley to confront him with any statement that he made while the Drayton-Acworth inquiry was in progress, or as to Mr. Chamberlin's evidence I suppose he could be called. That is what I would think.

"Mr. LAFLEUR: Subject to those observations, if you wish to have this report in as a sort of public document we have no serious objection, but if that

deposition, and these statements of the finances are to be relied on as evidence in this case then we say it is illegal and should not be admitted.

"Hon. Mr. TAFT: I do not think myself that the report is evidence.

"Mr. TILLEY: I am not tendering it in that light, but merely showing the report to be evidence of the facts stated. I am tendering it as one of the documents that has become public since the negotiations commenced about the Grand Trunk's difficulties with respect to the Grand Trunk Pacific and about the Government taking it over, and I put it forward because, in the report itself, there are certain recommendations made as to the treatment to be accorded to the Grand Trunk which it may be material for me to refer to when it comes to a summation of the case at the end, because my friends may rely on stock exchange quotations, and such like, and all these things would have a bearing, particularly under clause 20 of the agreement.

"The CHAIRMAN: Mr. Lafleur and you could agree.

"Mr. TILLEY: I think we substantially agree. The evidence of Mr. Kelley, putting it in that way, possibly is not evidence of the fact, but it is evidence to this extent, that a Commission was appointed to investigate matters, that they made certain requests to the Government, heard them and reached certain conclusions as to what they had to say with regard to their properties, and so on, but it hasn't any great bearing on the question of value.

"The letter Mr. Kelley wrote, however, is in a different category, because there he was answering specific questions and that we feel is in to stay."

But even if Mr. Chamberlain's statements are to be taken as evidence, in the nature of admissions against the shareholders, they should be given no weight to establish bankruptcy of the company then or later. The counsel for the Government have satisfactorily shown that the statements of Mr. Chamberlain were only a part of the plan to show the Grand Trunk to be in a worse condition than it was, of which the understatement of revenues to the extent of eight millions was another part, all with a view of threatening bankruptcy in the hope of inducing the Government to relieve the Grand Trunk of the burden of the Grand Trunk Pacific. It is not just to visit responsibility for such evidence upon innocent stockholders and thereby establish against them a probable bankruptcy which their directors really did not credit and were adopting most questionable methods for an ulterior purpose, to prove. These statements of Mr. Chamberlain were made in the year 1917 immediately after the most profitable year in the history of the Grand Trunk when its surplus, after paying all its fixed charges, was \$11,319,341, a sum large enough to pay the full guarantees on the Grand Trunk Pacific debentures, a dividend on the 4 per cent guaranteed stock, the dividends on the three preference stocks and leave a surplus of more than two million for extra maintenance. Instead of being in bankruptcy or near it at that time, the Grand Trunk Railway was more prosperous than ever in its history, but the directors were trying to conceal it. This shows how unfair it is in this proceeding to base our judgment on what Mr. Chamberlain said in 1917.

We come now to the past earnings and the probable future net earnings as the only evidence of value of this stock.

This subject requires a reference to the accounts of the Grand Trunk Railway Company of Canada. It appears without dispute that from 1912 until 1920, the London management exercised a discretion to understate operating revenues and to understate operating expenses with a view to making the published statements of the earnings and expenses of the railway different from that which a true transcript of the books would have disclosed. In doing this they made use of a so-called audit office account which they charged and credited with sums to accomplish their purpose. They directed these charges and credits by cable messages to Mr. Chamberlain and the

officer in charge of accounts. Counsel for the Government ascribe variable motives to the London management for this treatment of the accounts and they are borne out by the circumstances. In 1913 the operating revenues were improperly increased apparently in order to justify the declaration of a dividend on the three series of preferred stocks, a full dividend on the first and second, and half on the third. Then came a period in which the London management was anxious to induce the Canadian Government to take the burden of the Grand Trunk Pacific off its back, on the ground that obligation to run and finance the Pacific road might lead to the bankruptcy of the Grand Trunk. That led the London management to understate their operating revenues and charge the Audit Office Fund during the years 1915, 1916 and 1917 with an aggregate of nearly eight million dollars that should have appeared as additional revenue.

In 1919 and 1920, when the sale of the road to the Government was being faced as the best course, manipulation of the accounts was directed to making the financial condition of the road seem better than it was. This dealing with accounts by the London management admits of no defence, but it cannot be permitted to prejudice the interests of the shareholders in this case. The London management in these misleading statements was attempting to induce action on the part of the Government, on the one hand, and to avoid complaint on the part of the shareholders, on the other. The local officers, except the President and those immediately charged with the matter of accounts, were not privy to this action. This is not a proceeding to penalize managers or directors of a company for false statements. We must refer to it, however, in order to understand the necessity of restating the accounts and to reach the truth as to the real earnings of the Grand Trunk Railway Company of Canada during the ten years from 1910 to 1920.

The Chairman of the Board has referred to a statement by Mr. McLaren, the auditor, in respect to the accounts as published for 1919, in which year there was a deficit, according to the corrected accounts, of \$6,488,918.75, whereas the result as published was \$5,556.53. It should be added that this discrepancy arose from the fact that there was taken from the office audit account the amounts which had been withheld from operating revenues in 1916 and 1917, to the extent of more than \$7,000,000, and put, with the exception of about \$150,000, into maintenance of way and maintenance of equipment, and used it in the betterment of the road in 1919, but in the published account for 1919 was not shown. In other words, the fund created by the understatement of operating revenues in 1915, 1916 and 1917 was used as a reserve account for renewals and repairs of the road in 1919, but the published accounts showed neither the formation of the reserve nor its expenditure.

Another feature of the accounts which is misleading and which became quite material after 1916, was entering to the credit of the company, as if paid, interest which was not paid on advances made to the Grand Trunk Pacific and to other subsidiary companies, on advances made for the purchase of land for use in the future which was wholly unremunerative. In some cases it represented a reasonable expectation of future payment, but in other cases it was an obligation, notably in the case of the Grand Trunk Pacific Company and in the case of the Grand Trunk Pacific Branch Lines Company, entirely worthless, upon which nothing could ever be realized. The books have been revised by Mr. McLaren to eliminate the two features referred to of the audit office account, and the other overstatements and understatements, and the crediting of unpaid interest. The unpaid interest does not enter into the net operating income, but into the final surplus applicable to fixed charges and dividends.

I have attempted, in what I have had to say in this case to deal only with the accounts as revised by Mr. McLaren, the auditor, and they are, as I understand, undisputed.

From the revised accounts it appears that in the year 1910, the percentage of the operating surplus of the Grand Trunk Railway Company of Canada, after taxes,

uncollectable railway revenues, hire of equipment, joint facility rents, etc., were paid, was 26 per cent of the total operating expenses. I append, in tabular form, the showing as to 1910 and the following years:—

In 1910..	26 per cent
" 1911..	25 "
" 1912..	23 "
" 1913..	19.6 "
" 1914..	23.35 "
" 1915..	32 "
" 1916..	32.88 "
" 1917..	18 "
" 1918..	8.4 "
" 1919..	3.16 "
" 1920..	3.91 "

This table shows an average for the seven years before 1917, when the United States came into the war, of 25.97 per cent and justifies the claim of counsel that 25 per cent is a normal percentage of the net operating income of the Grand Trunk Railway. It is in accord with the normal percentage for many of the first-class railways of the country. Indeed it is in a percentage which has been recognized by the Railway Commission of Canada and other public bodies engaged in fixing rates, as a reasonable one. The reduction in the net operating income since 1918 is due to the enormous increase in the operating expenses, which have grown far more rapidly than the operating expenses, though they have increased, due both to growth of traffic and higher rates. The labour costs increased 100 per cent or more, and material in some respects quite as much. This feature was more marked after the armistice than during the war, so that under the award of railway boards, huge sums were imposed upon railways as back pay to their employees, and sometimes before any attempted compensating increase of rates had been allowed to go into effect. These were the features of the year 1920 which was so disastrous in railway circles. Railways which had up to that time always earned a normal surplus were put in the category of those not earning even their operating expenses. This is now changing. The tendency of all wages is now downward. The Railway Board of the United States ordered a decrease in the wages of the skilled railway employees of 12 per cent and more, effective July 1st last, and the percentage in reduction of common labour has been far in excess of this, with large numbers of unemployed. So, too, has the price of all material that enters into the operation of railways been much reduced, notably the price of coal. The returns of the American railways for the months of June and July, after the order reducing wages went into effect, indicate that the turn is at hand. How rapid the return to the normal will be is of course a matter of judgment, but the changes in the returns as the official reports for June and July, are so marked as to indicate that it will be only for two or three years before the normal ratio between operating expenses and operating revenues will be restored. This grows chiefly out of the reduction in operating expenses. The operating revenues show a decline, but the difference between the operating revenues and the operating expenses is broadening toward a wholesome net operating surplus for the railways.

Having this determined from the past what is the normal operating ratio of revenues to net operating surplus, we come now to consider what we may normally expect to be the sum of the operating revenues of the Grand Trunk Railway Company of Canada. These revenues increased from \$36,133,125 in 1910, to \$81,442,647 in 1920. The ton miles for freight traffic increased from 3,143,687,000 to 5,028,650,000, or at the rate for the ten years of 60 per cent or 6 per cent a year. The passenger traffic in 1911 was 545,335,000 miles, and in 1920, 529,810,000 passenger miles, showing a decrease during the ten years of 2.6 per cent. In other words, the passenger traffic was about stationary, while the freight traffic increased 6 per cent. The operating revenues for 1919 were nearly \$70,000,000. The operating revenues for 1920 were \$81,000,000. The operating revenues for the first four months of 1921—not a good year for business, and always the worst third of the year, because the

movements for grain are in the latter part of the year—was, in round numbers, \$23,500,000, from which we can properly calculate that the total revenues for 1921 are likely to reach at least \$72,000,000. It is fairer to take this as the basis of our calculation than \$81,000,000 in 1920, because the traffic that year was exceptional and the rates in 1920 were higher than the rates in 1921, which latter rates seem quite likely to continue. Beginning therefore with the basis of \$72,000,000 of business, and allowing for an increase of 5 per cent a year, at the end of 1926, five years hence, we should have a total of \$90,000,000. Assuming that the normal operating ratio of 25 per cent will be restored by that time, it would make the net operating surplus applicable to fixed charges, and other liabilities, and to the payment of dividends on capital stock, \$22,500,000 for 1926.

We now turn to the fixed charges. The statement put in by the Government shows that the funded obligations of the Grand Trunk Railway Company of Canada, including its own direct indebtedness, the funded obligations of its stock, controlled and leased lines, which it has paid in the past when the principal debtor failed to pay, amounts after excluding the Grand Trunk Pacific guarantees, to \$17,421,455.88. This includes interest on an issue of 25 millions of dollars in 1920, bearing 7 per cent interest to take up obligations incurred in meeting the deficit. It also includes the 4 per cent dividend on the guaranteed stock. The Grand Trunk Pacific guarantee by the Grand Trunk Railway of Canada should be stated in two amounts. The first is its absolute guaranty of \$2,291,660. Its conditional guaranty is \$1,395,000. To this should be added the cost of refunding 4, 5 and 6 per cent bonds which fall due in 1922, amounting to \$297,200. The Grand Trunk and the subsidiary lines after the disastrous years of 1920, 1919, and 1918, as is shown by the unpaid vouchers needed some \$18,000,000, \$14,000,000 for the Grand Trunk and \$4,000,000 for the United States lines for an operating cash or working fund upon which interest due for the year 1921, amounts to \$858,031 for the Grand Trunk lines and \$254,122 for the other lines. Another item which Mr. Brown, the government accountant, inserted in his statement, and which appears in the budget, was for something over \$5,000,000 as bank draft drawing interest. I eliminate that for the reason that as between the Grand Trunk Railway and the Government, the Government owes to the Grand Trunk something over \$5,000,000, being a sum which it received as the proceeds of the Grand Trunk twenty-five million, 1920 loan, by reason of a profit on exchange which it made in paying off obligations of the Grand Trunk in London. This, therefore, I state in tabular form below, making a total of \$22,467,468.88.

Funded obligations of the Grand Trunk Railway Company of Canada, including its own direct indebtedness, the funded obligations of its stock controlled, and leased lines which it has paid in the past when the primary debtor failed to pay, excepting the Grand Trunk Pacific, and including the 4 per cent guaranteed stock.. . . .	\$17,421,455.88
Grand Trunk Pacific absolute guaranty.. . . .	2,291,660.00
Grand Trunk Pacific conditional guaranty.. . . .	1,395,000.00
Refunding 4, 5 and 6 per cent bonds which fall due in 1922.. . . .	297,200.00
The deficit of the Grand Trunk and the subsidiary lines during the disastrous years of 1920, 1919 and 1918, amounting to \$18,000,000, upon which interest will be due in 1921, amounts to \$858,031 for the Grand Trunk lines, and \$254,122 for the other lines, or a total of.. . . .	1,112,153.00
Total.. . . .	\$22,467,468.88
From this should be deducted the non-operating income which appears upon Mr. McLaren's Exhibit to be for the year 1920.. . . .	\$3,122,505.00
From that, however, should be deducted for interest credited to the Grand Trunk, which was not paid.. . . .	1,179,821.00
Leaving a balance for non-operating income even in that bad year of.. . . .	\$1,942,648.00
In the same year Mr. McLaren credits the Grand Trunk for surplus income of subsidiary companies even in that year.. . . .	449,532.00
	2,392,216.00
This leaves as the <u>fixed charges to be provided for</u>	\$20,075,252.00
Deducting this from the net estimated operating income in 1926, amounting to \$23,400,000, it leaves.. . . .	3,324,748.00

which is enough to pay the \$2,424,748 or within \$150,000 of the limit fixed under the contract beyond which this Award cannot go.

I have been dealing only with the unit of the Grand Trunk Railway of Canada, and not with the lines going to make up the Grand Trunk System. They have had deficits which have been taken care of by the Grand Trunk in the past and in the statement of fixed charges given above. This is true also of the Vermont Central which is not in the System, but whose bonded indebtedness is included in the statement of funded obligations of the Grand Trunk stated above. Now these parts of the Grand Trunk System and the Vermont Central are bound to share in the improvement growing out of a return to a more normal relation of operating revenues to operating net income. They have in the past generally paid their fixed charges, some of them have paid dividends, and there is no reason why they may not in a reasonably short time come to do so again. When they do meet their fixed charges, they will relieve the Grand Trunk of an annual payment of \$1,312,649, as follows:—

Portland Elevator Company.. . . .	\$ 11,075
Grand Trunk Western Railway.. . . .	655,024
Milwaukee Ferry Company.. . . .	1,890
Central Vermont Railway.. . . .	507,635
Rail and River Coal Company.. . . .	97,025
Montreal Warehousing Company.	40,000
	<hr/>
	\$1,312,649

This will give leeway for making of capital expenditures in improving the railroad system without excluding these Grand Trunk shareholders from participating in the benefit of better times.

In addition to this, the subsidiary companies belonging to the Grand Trunk, whose undistributed surpluses are credited above, may well in a period of good times increase both their dividends which would increase the non-operating income as well as their undistributed surpluses.

In stating this conclusion, I am met by the inquiry, "Assuming your estimates to be correct, what are you to do in the meantime, and how are the probable deficits to be prevented from piling up in such a way as to create permanent fixed liabilities absorbing this net operating income which you assume for the year 1926?" It should be noted in the first place that from the total fixed charges stated in tabular form in the foregoing amounting to \$22,467,468.88, reduced by the non-operating income and by the surplus income of subsidiary lines to \$20,075,252, there is included conditional obligations that do not arise until there are not earnings over fixed charges. They are not cumulative, and the failure to pay them would not constitute a deficit increasing the funded or unfunded indebtedness.¹

These are the amounts due on the guaranteed stock.. . . .	\$2,433,333.33
and the conditional guaranty of the Grand Trunk Pacific of	1,395,000.00
	<hr/>
	\$3,828,333.33

Deducting this from the fixed charges of \$20,075,252 leaves \$16,246,918.67, as the fixed charges to be met during the interval before the net earnings are enough to pay anything on the guaranteed stock or the smaller conditional Grand Trunk Pacific guaranty. Twenty per cent net operating income on 81 millions would meet all the absolute fixed charges and this result we may anticipate within two or three years. Assuming that after the proper maintenance for the year 1922 there may be a deficit, and that deficits continue so as to make an addition to the permanent liabilities of \$10,000,000, this would add \$700,000 to the fixed charges which could be met as above and still leave the limit for the stockholders in 1926. The recent experiences of some American railways, as already indicated, show that this normal ratio may not be

postponed for six years, but may come in considerably less time than that, and that the current deficits will have disappeared long before 1926, so that the surplus will begin to afford a part payment on capital stock.

What might have happened to this road had the Government not taken it over and adopted the policy it has of very large investment for capital betterment and extraordinary maintenance, is of course a matter of judgment for the arbitrators. Five years is not a long time in which to calculate ahead. Such calculations must be made in determining the potential values of property subject to such change as this is.

The stock upon which dividends may not be paid for five years is not as valuable as that upon which they are paid at once and this may properly reduce the amount immediately to be awarded below the value of the stock in 1926, as above stated. As I am in the minority, however, and my conclusion is not to be embodied in an award, I need not discuss how much reduction should be made for this postponement, though it ought certainly not to be more than twenty-five per cent. This would make my appraisalment of all the stock, the value of which is here in issue, not less than forty-eight million dollars.

For the reasons given I must dissent from my brethren.

